Supreme Court, U.S.
FILED

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No. 03-___

In The

Supreme Court of the United States

CIGNA HEALTHCARE OF CALIFORNIA, INC.,

Petitioner,

vs.

MUZEYYEN BALABAN-ZILKE, Ph.D., individually and as successor-in-interest to BRAD ZILKE,

Respondent.

On Petition For A Writ Of Certiorari To The Court Of Appeal Of California, Second Appellate District

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The Federal Arbitration Act provides that an arbitration agreement "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Contrary to the Federal Arbitration Act, California Health and Safety Code section 1363.1 (West 2003) imposes four separate disclosure requirements for arbitration agreements in health care plans that are *not* requirements generally applicable to all contracts, and are therefore preempted absent a countervailing federal law that defeats preemption. *See Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 686-87 (1996). The McCarran-Ferguson Act provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State *for the purpose of regulating the business of insurance* . . . unless such Act *specifically relates to the business of insurance*." 15 U.S.C. § 1012(b) (emphasis added).

The questions presented by this case are:

(1) Whether the McCarran-Ferguson Act saves state laws that impose special requirements on arbitration agreements in insurance plans, such as California Health and Safety Code section 1363.1, from preemption by the Federal Arbitration Act? There is a wide split in authority on this recurring question.

(2) Whether this Court should resolve the following circuit splits involving the interpretation of the McCarran-Ferguson Act:

QUESTIONS PRESENTED – Continued

(a) Can a federal law "specifically relate[ ] to the business of insurance," and thus preempt contrary state insurance law even if the federal law does not refer to insurance in its text?

(b) Is the three-factor test set forth in *Group Life and Health Insurance Co. v. Royal Drug Co.*, 440 U.S. 205 (1979) and *Union Labor Life Insurance Co. v. Pireno*, 458 U.S. 119 (1982) used to determine whether a state law was enacted "for the purpose of regulating the business of insurance," and if so, to what extent?

(c) Should the two-part test set forth by this Court last term in *Kentucky Ass'n of Health Plans v. Miller*, 123 S. Ct. 1471, 1477-78 (2003) be extended to apply to the McCarran-Ferguson Act?

PARTIES TO THE PROCEEDINGS BELOW

All parties to the proceedings below are included in the caption except for defendants Medipace Medical Group Inc. and Victor Gura, M.D., who have not sought additional review of the order denying enforcement of their separate and different arbitration agreement.

RULE 29.6 STATEMENT

CIGNA HealthCare of California, Inc. is a wholly owned subsidiary of Healthsource, Inc. Healthsource, Inc. is a wholly owned subsidiary of CIGNA Health Corporation. CIGNA Health Corporation is a wholly owned subsidiary of Connecticut General Corporation. Connecticut General Corporation is a wholly owned subsidiary of CIGNA Holdings, Inc. CIGNA Holdings, Inc. is a wholly owned subsidiary of CIGNA Corporation. CIGNA Corporation is a public company, traded on the New York Stock Exchange and other exchanges. No one publicly held company owns 10% or more of the stock of CIGNA Corporation.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	
PARTIES TO THE PROCEEDINGS BELOW	iii
RULE 29.6 STATEMENT	iii
TABLE OF AUTHORITIES	vii
PETITION FOR A WRIT OF CERTIORARI	1
OPINIONS BELOW	1
JURISDICTION	1
CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED	2
STATEMENT OF THE CASE	3
A. Factual and procedural background	3
B. The split in authority regarding the interplay between the McCarran-Ferguson Act and the FAA	5
C. The split in authority regarding whether a state insurance law is saved from federal preemption by the McCarran-Ferguson Act	8
1. Split in authority on the interpretation of whether a federal law "specifically relates" to insurance	8
2. Split in authority over when a state law has been enacted "for the purpose of regulating the business of insurance"	9
3. New two-part test from *Kentucky Ass'n of Health Plans v. Miller*	11

TABLE OF CONTENTS – Continued

Page

REASONS FOR GRANTING THE WRIT 12

CERTIORARI SHOULD BE GRANTED TO RESOLVE CIRCUIT CONFLICTS OVER THE INTERPLAY BETWEEN THE MCCARRAN-FERGUSON ACT AND THE FEDERAL ARBITRATION ACT 12

A. Certiorari is necessary to resolve the split among state and federal courts over whether the FAA preempts state laws that impose special requirements on arbitration agreements in healthcare or insurance plans 12

1. The FAA policy in favor of enforcing arbitration agreements and the McCarran-Ferguson Act's goal of limiting federal control over insurance law collide when states impair arbitration clauses in insurance contracts 12

2. There is a split in authority on the question of whether and when the McCarran-Ferguson Act saves state laws affecting arbitration clauses from FAA preemption ... 14

B. Independent of the FAA-specific question presented in this case, certiorari is necessary to resolve various circuit splits over interpretation of the McCarran-Ferguson Act 17

1. There is a circuit split over the determination of when a federal statute "specifically relates to the business of insurance" 17

a. This Court has not fully resolved the meaning of "specifically relates" as used in the McCarran-Ferguson Act 17

TABLE OF CONTENTS – Continued

Page

b. Some courts have held that a federal law can preempt a state insurance law even if the federal law does not refer to insurance in its text 18

c. Other courts, including the Court of Appeal here, have held that if the text of a federal law does not refer to insurance, then it cannot "specifically relate to insurance" 20

2. There is a circuit split over the effect *Fabe* had on the three-factor test set forth in *Royal Drug* and *Pireno* for non-antitrust cases 21

a. This Court has not set forth a clear test for when state laws regulate the "business of insurance" in non-antitrust cases 21

b. Some courts have held that *Fabe* precludes use of the *Royal Drug* and *Pireno* test in first clause cases 23

c. Other courts have held that the *Royal Drug* and *Pireno* three-factor test applies in first clause cases 24

d. The circuits that apply the *Royal Drug* and *Pireno* test in non-antitrust first clause cases are split over how the test applies 25

3. This Court should grant certiorari to hold that the new two-part test set forth in *Kentucky Ass'n of Health Plans, Inc. v. Miller* applies in McCarran-Ferguson Act cases 27

CONCLUSION 30

TABLE OF AUTHORITIES

Page

CASES

Ainsworth v. Allstate Ins. Co., 634 F. Supp. 52 (W.D. Mo. 1985) 7

Allen v. Pacheco, 71 P.3d 375 (Colo. 2003) 7

Am. Bankers Ins. Co. of Fla. v. Crawford, 757 So.2d 1125 (Ala. 1999) 7, 14, 15

Am. Deposit Corp. v. Schacht, 84 F.3d 834 (7th Cir. 1996) 9, 25, 29

Am. Heritage Life Ins. Co. v. Orr, 294 F.3d 702 (5th Cir. 2002) 6

In re Arbitration of Mut. Reinsurance Bureau v. Great Plains Mut. Ins. Co., 750 F. Supp. 455 (D. Kan. 1990) 7, 15

In re Arbitration of Mut. Reinsurance Bureau v. Great Plains Mut. Ins. Co., 969 F.2d 931 (10th Cir. 1992) 7, 15

Autry v. Northwest Premium Servs., Inc., 144 F.3d 1037 (7th Cir. 1998) 10, 26, 27

Barnett Bank of Marion County, N.A. v. Nelson, 517 U.S. 25 (1996) 13, 17

Bennett v. Liberty Nat'l Fire Ins. Co., 968 F.2d 969 (9th Cir. 1992) 6

Bernstein v. Centaur Ins. Co., 606 F. Supp. 98 (S.D.N.Y. 1984) 7, 19

Blackfeet Nat'l Bank v. Nelson, 171 F.3d 1237 (11th Cir. 1999) 8, 20

Bullock v. United Benefit Life Ins. Co., 165 F. Supp. 2d 1259 (M.D. Ala. 2001) 7, 15

TABLE OF AUTHORITIES – Continued

Page

Celtic Life Ins. Co. v. McLendon, 814 So.2d 222 (Ala. 2001) 7

Citizens Bank v. Alafabco, Inc., 123 S. Ct. 2037 (2003) 13

Cochran v. Paco, Inc., 606 F.2d 460 (5th Cir. 1979) 8, 13, 21

Cont'l Ins. Co. v. Equity Residential Props. Trust, 255 Ga. App. 445, 565 S.E.2d 603 (2002) 7, 15

Costle v. Freemont Indem. Co., 839 F. Supp. 265 (D. Vt. 1993) 7

Cox v. Woodmen of the World Ins. Co., 347 S.C. 460, 556 S.E.2d 397 (2001) 7, 15

Davister Corp. v. United Republic Life Ins. Co., 152 F.3d 1277 (10th Cir. 1998) 7

DiMercurio v. Sphere Drake Ins., PLC, 202 F.3d 71 (1st Cir. 2000) 6, 15

Doctor's Assocs., Inc. v. Casarotto, 517 U.S. 681 (1996) 6, 12

Doe v. Norwest Bank Minn., N.A., 107 F.3d 1297 (8th Cir. 1997) 10, 24

Eden Fin. Group, Inc. v. Fidelity Bankers Life Ins. Co., 778 F. Supp. 278 (E.D. Va. 1991) 7

Friday v. Trinity Universal of Kan., 262 Kan. 347, 939 P.2d 869 (1997) 7, 15

Group Life and Health Insurance Co. v. Royal Drug Co., 440 U.S. 205 (1979) ..... *passim*

Hamilton Life Ins. Co. of N.Y. v. Republic Nat'l Life Ins. Co., 408 F.2d 606 (2d Cir. 1969) 7, 15

TABLE OF AUTHORITIES – Continued

Page

Hart v. Orion Ins. Co., 453 F.2d 1358 (10th Cir. 1971) 6

Humana Inc. v. Forsyth, 525 U.S. 299 (1999) 10

Imbler v. PacifiCare of Cal., Inc., 103 Cal. App. 4th 567, 126 Cal. Rptr. 2d 715 (2002) ..... *passim*

Kentucky Ass'n of Health Plans v. Miller, 123 S. Ct. 1471 (2003) 11

Lander v. Hartford Life & Annuity Ins. Co., 251 F.3d 101 (2d Cir. 2001) 19

Life of Am. Ins. Co. v. Aetna Life Ins. Co., 744 F.2d 409 (5th Cir. 1984) 6

In re Liquidation of Union Indem. Ins. Co. of N.Y., 137 Misc. 2d 575, 521 N.Y.S.2d 617 (1987) 7

Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995) 12

Md. Cas. Co. v. Cushing, 347 U.S. 409 (1954) 20

Merchs. Home Delivery Serv., Inc. v. Hall & Co., 50 F.3d 1486 (9th Cir. 1995) 9, 10, 24, 26, 29

Miller v. Nat'l Fid. Life Ins. Co., 588 F.2d 185 (5th Cir. 1979) 6, 27, 28, 29

Murff v. Prof'l Med. Ins. Co., 97 F.3d 289 (8th Cir. 1996) 8, 21

NAACP v. Am. Family Mut. Ins. Co., 978 F.2d 287 (7th Cir. 1992) 8, 21

Owensboro Nat'l Bank v. Stephens, 44 F.3d 388 (6th Cir. 1994) 9, 24, 25

PacifiCare Health Sys., Inc. v. Book, 123 S. Ct. 1531 (2003) 13

TABLE OF AUTHORITIES – Continued

Page

Pagarigan v. Superior Court, 102 Cal. App. 4th 1121, 126 Cal. Rptr. 2d 124 (2002) 7

Patenaude v. Equitable Life Assurance, 290 F.3d 1020 (9th Cir. 2002) 13

Preziose v. Lumbermen's Mut. Cas. Co., 152 Vt. 604, 568 A.2d 397 (1989) 7

Quackenbush v. Allstate Ins. Co., 121 F.3d 1372 (9th Cir. 1997) 6

Rush Prudential HMO, Inc. v. Moran, 536 U.S. 355 (2002) 5

SEC v. Nat'l Sec., 393 U.S. 453 (1969) 13, 22

Sabo v. Met. Life Ins. Co., 137 F.3d 185 (3d Cir. 1998) 9, 25, 26

Sears, Roebuck & Co. v. All States Life Ins. Co., 246 F.2d 161 (5th Cir. 1957) 20

Smith v. PacifiCare Behavioral Health of Cal., Inc., 93 Cal. App. 4th 139, 113 Cal. Rptr. 2d 140 (2001) ..... *passim*

Spirt v. Teachers Ins. & Annuity Ass'n, 735 F.2d 23 (2d Cir. 1984) 18

Spirt v. Teachers Ins. & Annuity Ass'n, 691 F.2d 1054 (2d Cir. 1982) 18, 19

St. Paul Fire & Marine Ins. Co. v. Courtney Enters., Inc., 270 F.3d 621 (8th Cir. 2001) 6

Standard Sec. Life Ins. Co. of N.Y. v. West, 267 F.3d 821 (8th Cir. 2001) 7, 15

Stephens v. Am. Int'l Ins. Co., 66 F.3d 41 (2d Cir. 1995) 7

TABLE OF AUTHORITIES – Continued

Page

Stephens v. Nat'l Distillers & Chem. Corp., 69 F.3d 1226 (2d Cir. 1995) 8, 18, 19

Teachers Ins. & Annuity Ass'n v. Spirt, 463 U.S. 1223 (1983) 18

Towe, Hester & Erwin, Inc. v. Kan. City Fire & Marine Ins. Co., 947 P.2d 594 (Okla. Ct. App. 1997) 7, 15

Union Labor Life Insurance Co. v. Pireno, 458 U.S. 119 (1982) ..... *passim*

United States Department of the Treasury v. Fabe, 508 U.S. 491 (1993) ..... *passim*

Washburn v. Corcoran, 643 F. Supp. 554 (S.D.N.Y. 1986) 7

Zolezzi v. PacifiCare of Cal., 105 Cal. App. 4th 573, 129 Cal. Rptr. 2d 526 (2003) 7

CONSTITUTIONS

United States Constitution art. VI, cl. 2 ..... 2, 12

STATUTES

9 U.S.C. § 2 ..... 2, 8, 12

15 U.S.C. § 1012(b) ..... *passim*

28 U.S.C. § 1257(a) 1

29 U.S.C. § 1144(b)(2)(A) 11

Alaska Stat. § 09.55.535 (Michie 2003) 5

California Civil Procedure Code § 1295 (West 2003) 3

TABLE OF AUTHORITIES – Continued

Page

California Health & Safety Code § 1363.1 (West 2000) 2, 4, 5, 6, 29

Colorado Rev. Stat. § 13-64-403 (2003) 5

Georgia Code Ann. § 9-9-2(c)(3) (Michie 2003) 5

Kansas Stat. Ann. § 5-401(c)(1) (2002) 5

710 Illinois Comp. Stat. Ann. 15/9 (West 2003) 5

Louisiana Rev. Stat. Ann. § 9:4235 (West 2003) 5

Massachusetts Gen. Laws ch. 175, § 22 (2003) 5

Maine Rev. Stat. Ann. tit. 24-A, § 2747 (West 2003) 5

Missouri Rev. Stat. § 435.350 (2003) 5

Nevada Rev. Stat. § 689B.067 (2003) 5

Ohio Rev. Code Ann. § 2711.23-2711.24 (Anderson 2003) 5

Oklahoma Stat. tit. 15, § 802 (2003) 5

Rhode Island Gen. Laws § 10-3-2 (2002) 5

South Carolina Code Ann. § 15-48-10 (Law Co-op. 2002) 5

South Dakota Codified Laws § 21-25B-3 (Michie 2003) 5

Texas Rev. Civ. Stat. Ann. art. 4590i (Vernon 2003) 5

Utah Code Ann. § 78-14-17 (2003) 5

Vermont Stat. Ann. tit. 12, § 5653 (2003) 5

Virginia Code Ann. § 38.2-5803 (Michie 2003) 5

TABLE OF AUTHORITIES – Continued

Page

MISCELLANEOUS

Kristen Angus, *Tenth Circuit Surveys: Arbitration*, 76 DENV. U. L. REV. 681 (1999).....14, 16

Willy E. Rice, *Federal Courts and the Regulation of the Insurance Industry: An Empirical and Historical Analysis of Courts' Ineffectual Attempts to Harmonize Federal Antitrust, Arbitration, and Insolvency Statutes with the McCarran-Ferguson Act – 1941-1993*, 43 CATH. U. L. REV. 399 (1994).....16

Peter B. Steffen, *After Fabe: Applying the Pireno Definition of 'Business of Insurance' in First-Clause McCarran-Ferguson Act Cases*, U. CHI. LEGAL F. 447 (2003).....23

Jennifer Nicole Taylor, *Recent Development: Erickson v. Aetna Health Plans of California, Inc.: When the Federal Arbitration Act Closes One Courtroom Door, Let the McCarran-Ferguson Act Open Another*, 28 W. ST. U. L. REV. 257 (2000).....15

PETITION FOR A WRIT OF CERTIORARI

CIGNA HealthCare of California, Inc. (CHC) respectfully petitions for a writ of certiorari to review the decision of the Court of Appeal of California, Second Appellate District, in this case.

OPINIONS BELOW

The unreported February 10, 2000 order of the Superior Court of the State of California, Los Angeles County denying CHC's petition to compel arbitration is reproduced in the appendix (App.) at 25-29. The unreported May 19, 2000 order of the Superior Court denying CHC's motion for reconsideration is reproduced at App. 30-34. The unreported May 28, 2003 opinion of the Court of Appeal of the State of California, Second Appellate District, Division Four is reproduced at App. 1-23. The unreported June 24, 2003 order of the Court of Appeal denying petitioner's petition for rehearing is reproduced at App. 24. The unreported August 13, 2003 order of the Supreme Court of California denying petitioner's petition for review from the Court of Appeal's May 28, 2003 opinion is reproduced at App. 35.

JURISDICTION

The California Court of Appeal decision that is the subject of this petition was entered on May 28, 2003. App. 1-23. On August 13, 2003, the California Supreme Court denied petitioner's timely petition for review. App. 35. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Supremacy Clause of the Constitution provides in relevant part: "[T]he Laws of the United States . . . shall be the supreme Law of the Land. . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. art. VI, cl. 2.

The Federal Arbitration Act provides in relevant part: "A written provision in any . . . contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or equity for the revocation of any contract." 9 U.S.C. § 2.

The McCarran-Ferguson Act provides in relevant part: "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act . . . known as the Sherman Act . . . and the Act . . . known as the Clayton Act, and the Act . . . known as the Federal Trade Commission Act . . . shall be applicable to the business of insurance to the extent that such business is not regulated by state law." 15 U.S.C. § 1012(b).

California Health and Safety Code section 1363.1 (West 2000) provides: "Any health care service plan that includes terms that require binding arbitration to settle disputes and that restrict, or provide for a waiver of, the right to a jury trial shall include, in clear and understandable language, a disclosure that meets all of the following conditions:

(a) The disclosure shall clearly state whether the plan uses binding arbitration to settle disputes, including specifically whether the plan uses binding arbitration to settle claims of medical malpractice.

(b) The disclosure shall appear as a separate article in the agreement issued to the employer group or individual subscriber and shall be prominently displayed on the enrollment form signed by each subscriber or enrollee.

(c) The disclosure shall clearly state whether the subscriber or enrollee is waiving his or her right to a jury trial for medical malpractice, other disputes relating to the delivery of service under the plan, or both, and shall be substantially expressed in the wording provided in subdivision (a) of Section 1295 of the Code of Civil Procedure.

(d) In any contract or enrollment agreement for a health care service plan, the disclosure required by this section shall be displayed immediately before the signature line provided for the representative of the group contracting with a health care service plan and immediately before the signature line provided for the individual enrolling in the health care service plan."

STATEMENT OF THE CASE

A. Factual and procedural background.

In this case, plaintiff Muzeyyen Balaban-Zilke (Balaban) enrolled herself and her future husband, Brad Zilke, in a CHC group health plan.[1] App. 2. The plan contained a mandatory arbitration provision. App. 3. Zilke obtained treatment under the plan and later died. *Id.* Balaban then

[1] In this brief we refer to plaintiff and respondent Muzeyyen Balaban-Zilke in the singular, although she sued CHC both individually and as the successor-in-interest to her deceased husband.

commenced this wrongful death action in the Los Angeles Superior Court against CHC and other defendants. App. 2-3.

CHC filed a petition to compel arbitration of Balaban's dispute. App. 3. The trial court denied CHC's petition because it found that CHC's arbitration agreement did not meet all of the disclosure requirements of California Health and Safety Code section 1363.1, pertaining exclusively to arbitration agreements contained in healthcare plans. App 28. CHC appealed, arguing that the Federal Arbitration Act (FAA) preempts section 1363.1. The Court of Appeal disagreed and affirmed.[2] App. 5-14.

In reaching its decision, the Court of Appeal relied almost exclusively on two recent published California Court of Appeal decisions – *Smith v. PacifiCare Behavioral Health of Cal., Inc.*, 93 Cal. App. 4th 139, 113 Cal. Rptr. 2d 140 (2001) and *Imbler v. PacifiCare of Cal., Inc.*, 103 Cal. App. 4th 567, 126 Cal. Rptr. 2d 715 (2002). App. 7-10. *Smith* and *Imbler* both held that the FAA does not preempt section 1363.1's special requirements for arbitration agreements in healthcare plans because of the reverse-preemption effect of the McCarran-Ferguson Act. *Imbler*, 103 Cal. App. 4th at 569, 126 Cal. Rptr. 2d at 717; *Smith*, 93 Cal. App. 4th at 143-44, 113 Cal. Rptr. 2d at 142-44.

CHC filed a petition for rehearing in the Court of Appeal, which the Court of Appeal denied. App. 24. CHC

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[2] The trial court provided a number of reasons why it would not enforce CHC's arbitration agreement. App. 26-29. CHC challenged all of those reasons on appeal. However, the Court of Appeal affirmed the trial court's order based solely upon the arbitration agreement's non-compliance with section 1363.1, and the failure of the FAA to preempt that state law. App. 4-5. The opinion thus cleanly presents a question of federal statutory construction squarely within this Court's jurisdiction.

then filed a petition for review in the California Supreme Court, which the Supreme Court denied. App. 35. This petition follows.

B. The split in authority regarding the interplay between the McCarran-Ferguson Act and the FAA.

This case presents one of the most important issues facing the healthcare and insurance industries today: whether states can impose unique restrictions on the enforcement of mandatory arbitration provisions in healthcare or insurance plans.[3] Numerous states have passed laws that either prohibit the enforcement of such arbitration agreements altogether, or impose special requirements on them before they can be judicially enforced.[4] This issue has generated a wave of litigation over whether these unique restrictions on arbitration agreements in healthcare or insurance plans are preempted by the FAA, which is designed to prevent states from

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[3] This Court has held that healthcare plans are a form of insurance. *See Rush Prudential HMO, Inc. v. Moran*, 536 U.S. 355, 367 (2002).

[4] *E.g.*, Alaska Stat. § 09.55.535 (Michie 2003); Cal. Health & Safety Code § 1363.1 (West 2000); Colo. Rev. Stat. § 13-64-403 (2003); Ga. Code Ann. § 9-9-2(c)(3) (Michie 2003); Kan. Stat. Ann. § 5-401(c)(1) (2002); 710 Ill. Comp. Stat. Ann. 15/9 (West 2003); La. Rev. Stat. Ann. § 9:4235 (West 2003); Mass. Gen. Laws ch. 175, § 22 (2003); Me. Rev. Stat. Ann. tit. 24-A, § 2747 (West 2003); Mo. Rev. Stat. § 435.350 (2003); Nev. Rev. Stat. § 689B.067 (2003); Ohio Rev. Code Ann. § 2711.23-2711.24 (Anderson 2003); Okla. Stat. tit. 15, § 802 (2003); R.I. Gen. Laws § 10-3-2 (2002); S.C. Code Ann. § 15-48-10 (Law Co-op. 2002); S.D. Codified Laws § 21-25B-3 (Michie 2003); Tex. Rev. Civ. Stat. Ann. art. 4590i (Vernon 2003); Utah Code Ann. § 78-14-17 (2003); 12 Vt. Stat. Ann. tit. 12, § 5653 (2003); Va. Code Ann. § 38.2-5803 (Michie 2003).

imposing special rules on arbitration agreements that are not applied to contracts generally.

There is no dispute that the FAA, by itself, would preempt all such state laws, including California Health and Safety Code section 1363.1, that impose unique restrictions on arbitration agreements. In *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996), this Court held that a Montana statute declaring an arbitration clause to be unenforceable unless notice of the arbitration issue was typed in underlined capital letters on the first page of the contract was preempted by the FAA because "generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening" the FAA, but state laws applicable only to arbitration provisions may not. *Id.* at 686-87.

The McCarran-Ferguson Act, however, prevents the preemption of a state law by another federal law if the state law was enacted "for the purpose of regulating the business of insurance" unless the other federal law "specifically relates to the business of insurance." 15 U.S.C. § 1012(b). The courts that have considered the relationship between the McCarran-Ferguson Act and the FAA are in conflict. Some courts have found that the FAA preempts state laws that target arbitration agreements in insurance plans[5] and other courts, like the California Court of Appeal

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[5] *E.g.*, *Am. Heritage Life Ins. Co. v. Orr*, 294 F.3d 702, 708-09 (5th Cir. 2002); *St. Paul Fire & Marine Ins. Co. v. Courtney Enters., Inc.*, 270 F.3d 621, 625 (8th Cir. 2001); *DiMercurio v. Sphere Drake Ins., PLC*, 202 F.3d 71, 75-81 (1st Cir. 2000); *Quackenbush v. Allstate Ins. Co.*, 121 F.3d 1372, 1381 (9th Cir. 1997); *Bennett v. Liberty Nat'l Fire Ins. Co.*, 968 F.2d 969, 972-73 (9th Cir. 1992); *Life of Am. Ins. Co. v. Aetna Life Ins. Co.*, 744 F.2d 409, 411-13 (5th Cir. 1984); *Miller v. Nat'l Fid. Life Ins. Co.*, 588 F.2d 185, 187 (5th Cir. 1979); *Hart v. Orion Ins. Co.*, 453

(Continued on following page)

in this case, have found that such laws are saved from FAA preemption by the McCarran-Ferguson Act.[6]

F.2d 1358, 1360 (10th Cir. 1971); *Hamilton Life Ins. Co. of N.Y. v. Republic Nat'l Life Ins. Co.*, 408 F.2d 606, 610-11 (2d Cir. 1969); *Bullock v. United Benefit Life Ins. Co.*, 165 F. Supp. 2d 1259, 1261-62 (M.D. Ala. 2001); *Costle v. Freemont Indem. Co.*, 839 F. Supp. 265, 274-75 (D. Vt. 1993); *In re Arbitration of Mut. Reinsurance Bureau v. Great Plains Mut. Ins. Co.*, 750 F. Supp. 455, 459-62 (D. Kan. 1990), *rev'd*, 969 F.2d 931 (10th Cir. 1992); *Ainsworth v. Allstate Ins. Co.*, 634 F. Supp. 52, 56-57 (W.D. Mo. 1985); *Bernstein v. Centaur Ins. Co.*, 606 F. Supp. 98, 101-03 (S.D.N.Y. 1984); *Celtic Life Ins. Co. v. McLendon*, 814 So.2d 222, 226 (Ala. 2001); *Am. Bankers Ins. Co. of Fla. v. Crawford*, 757 So.2d 1125, 1131-36 (Ala. 1999); *Allen v. Pacheco*, 71 P.3d 375, 388 (Colo. 2003) (Kourlis, J., dissenting) ("In short, I suggest that the interpretation the Majority affords the McCarran-Ferguson Act sweeps with a broad and wide arc that could swallow federal preemption under the Supremacy Clause."); *Towe, Hester & Erwin, Inc. v. Kan. City Fire & Marine Ins. Co.*, 947 P.2d 594, 597-99 (Okla. Ct. App. 1997); *Preziose v. Lumbermen's Mut. Cas. Co.*, 152 Vt. 604, 605-07, 568 A.2d 397, 398-99 (1989).

[6] *E.g.*, *Standard Sec. Life Ins. Co. of N.Y. v. West*, 267 F.3d 821, 823-24 (8th Cir. 2001); *Davister Corp. v. United Republic Life Ins. Co.*, 152 F.3d 1277, 1281-82 (10th Cir. 1998); *Stephens v. Am. Int'l Ins. Co.*, 66 F.3d 41, 45-46 (2d Cir. 1995); *In re Arbitration of Mut. Reinsurance Bureau v. Great Plains Mut. Ins. Co.*, 969 F.2d 931, 934-35 (10th Cir. 1992); *Eden Fin. Group, Inc. v. Fidelity Bankers Life Ins. Co.*, 778 F. Supp. 278, 282 (E.D. Va. 1991); *Washburn v. Corcoran*, 643 F. Supp. 554, 557-58 (S.D.N.Y. 1986); *Zolezzi v. PacifiCare of Cal.*, 105 Cal. App. 4th 573, 588 n.11, 129 Cal. Rptr. 2d 526, 539 n.11 (2003); *Imbler*, 103 Cal. App. 4th at 569, 126 Cal. Rptr. 2d at 717; *Pagarigan v. Superior Court*, 102 Cal. App. 4th 1121, 1133-34, 126 Cal. Rptr. 2d 124, 134-35 (2002); *Smith*, 93 Cal. App. 4th at 143-44, 113 Cal. Rptr. 2d at 142-44; *Allen*, 71 P.3d at 377; *Cont'l Ins. Co. v. Equity Residential Props. Trust*, 255 Ga. App. 445, 445, 565 S.E.2d 603, 604 (2002); *Friday v. Trinity Universal of Kan.*, 262 Kan. 347, 351-53, 939 P.2d 869, 872-73 (1997); *In re Liquidation of Union Indem. Ins. Co. of N.Y.*, 137 Misc. 2d 575, 579-81, 521 N.Y.S.2d 617, 620-21 (1987); *Cox v. Woodmen of the World Ins. Co.*, 347 S.C. 460, 466-68, 556 S.E.2d 397, 401-02 (2001).

C. The split in authority regarding whether a state insurance law is saved from federal preemption by the McCarran-Ferguson Act.

The lack of uniformity in decisions deciding whether the FAA preempts state insurance laws is symptomatic of a much larger conflict among the lower courts in their interpretation and application of the McCarran-Ferguson Act's reverse-preemptive effect on a broad range of federal laws other than the FAA.

1. Split in authority on the interpretation of whether a federal law "specifically relates" to insurance.

The McCarran-Ferguson Act preserves federal law preemption of a contrary state insurance law if that federal law "specifically relates to the business of insurance." 15 U.S.C. § 1012(b). There is a circuit split over the question of what constitutes a federal law that "specifically relates to the business of insurance." The Second and Eleventh Circuits have held that certain federal laws are so clearly intended to preempt all contrary state laws, including insurance laws, that it is immaterial if the federal law (like the FAA) does not refer to insurance in its text. *E.g.*, *Stephens v. Nat'l Distillers & Chem. Corp.*, 69 F.3d 1226, 1231 (2d Cir. 1995); *Blackfeet Nat'l Bank v. Nelson*, 171 F.3d 1237, 1244 n.10 (11th Cir. 1999).

In contrast, the Fifth, Seventh, and Eighth Circuits, like the court in this case, have held that if a federal law does not refer to insurance in its text, it necessarily does not "specifically relate" to insurance. *E.g.*, *Cochran v. Paco, Inc.*, 606 F.2d 460, 464 (5th Cir. 1979); *NAACP v. Am. Family Mut. Ins. Co.*, 978 F.2d 287, 294-95 (7th Cir. 1992); *Murff v. Prof'l Med. Ins. Co.*, 97 F.3d 289, 291 (8th Cir. 1996).

2. Split in authority over when a state law has been enacted "for the purpose of regulating the business of insurance."

The McCarran-Ferguson Act provides a state law, outside the antitrust context, can be saved from preemption by a contrary federal law if the state law was "enacted for the purpose of regulating the business of insurance." 15 U.S.C. § 1012(b). In *Group Life and Health Insurance Co. v. Royal Drug Co.*, 440 U.S. 205 (1979) and *Union Labor Life Insurance Co. v. Pireno*, 458 U.S. 119 (1982), this Court set forth a three-factor test for determining when a law regulates "the business of insurance" within the meaning of the McCarran-Ferguson Act provision governing antitrust laws. Since *Royal Drug* and *Pireno*, there has been a question in the lower courts as to whether this three-factor test applies in determining the applicability of the first clause of the McCarran-Ferguson Act in *non*-antitrust cases. In *United States Department of the Treasury v. Fabe*, 508 U.S. 491 (1993), this Court failed to resolve that question when it observed that *Royal Drug* and *Pireno* did not completely answer what is meant by the non-antitrust first clause of the McCarran-Ferguson Act. The lower courts, including the Court of Appeal in this case, therefore lack guidance on the appropriate test to use in non-antitrust cases when deciding whether a state law is preempted.

The Third, Sixth, Seventh, and Ninth Circuits have held that *Fabe* does not abrogate the use of the three-factor test from *Royal Drug* and *Pireno* in non-antitrust cases. *E.g.*, *Sabo v. Met. Life Ins. Co.*, 137 F.3d 185, 191 & n.3 (3d Cir. 1998); *Owensboro Nat'l Bank v. Stephens*, 44 F.3d 388, 391-92 (6th Cir. 1994); *Am. Deposit Corp. v. Schacht*, 84 F.3d 834, 840 (7th Cir. 1996); *Merchs. Home Delivery Serv., Inc. v. Hall & Co.*, 50 F.3d 1486, 1490 n.2 (9th Cir. 1995). Meanwhile the Eighth Circuit has held

that in such cases, *Fabe* completely abrogated the three-factor test's use. *E.g.*, *Doe v. Norwest Bank Minn., N.A.*, 107 F.3d 1297, 1305 n.8 (8th Cir. 1997), *overruled on other grounds*, *Humana Inc. v. Forsyth*, 525 U.S. 299, 305 n.6 & 314 (1999). Here, the Court of Appeal was not certain as to what test should be applied and adopted the reasoning in *Smith* that the *Royal Drug/Pireno* factors "are merely '*considerations* to be weighed.'" *Smith*, 93 Cal. App. 4th at 159, 113 Cal. Rptr. 2d at 155; *see also Imbler*, 103 Cal. App. 4th at 575, 126 Cal. Rptr. 2d at 722; App. 9-10 ("However, given the careful demonstrations in *Smith* and *Imbler* that section 1363.1 regulates the business of insurance under the *Pireno* test and other applicable criteria, we decline to revisit this issue.").

Even among lower courts that agree the *Royal Drug* and *Pireno* three-factor test should be used in non-antitrust cases, there is an additional circuit split over the relevance of whether the actual activity being regulated is part of the business of insurance. The Ninth Circuit has held that this factor is relevant, having the effect of limiting the McCarran-Ferguson Act's reverse preemptive effect. *E.g.*, *Merchs. Home Delivery Serv., Inc.*, 50 F.3d at 1489. But the Seventh Circuit has explicitly rejected the Ninth Circuit's approach and has held that courts should be concerned only with the purpose behind the state statute and not the regulated activity itself. *E.g.*, *Autry v. Northwest Premium Servs., Inc.*, 144 F.3d 1037, 1041 (7th Cir. 1998). Here, the Court of Appeal, by adopting the reasoning in *Smith* and *Imbler*, has accepted that the relevant focus is exclusively on the statute's purpose, so that the McCarran-Ferguson Act's reverse preemption saves an insurance-related state statute even if the conduct to which the statute is being applied does *not* itself relate to the business of insurance. *See Imbler*, 103 Cal. App. 4th at 574-77, 126 Cal. Rptr. 2d at 721-22; *Smith*, 93

Cal. App. 4th at 159-62, 113 Cal. Rptr. 2d at 155-56; *see also* App. 9-10.

3. New two-part test from *Kentucky Ass'n of Health Plans v. Miller*.

This case also presents an opportunity for this Court to "make a clean break from the McCarran-Ferguson factors" and apply instead the simpler two-part test that it adopted last term in *Kentucky Ass'n of Health Plans, Inc. v. Miller*, 123 S. Ct. 1471, 1479 (2003) in the ERISA context to determine whether "laws . . . regulate insurance" under 29 U.S.C. § 1144(b)(2)(A). The problems identified by this Court with the use of the *Royal Drug* and *Pireno* test in ERISA cases are also present in McCarran-Ferguson Act cases.

Under the two-part test articulated in *Miller*, the Court of Appeal's decision here, finding that section 1363.1 has the "purpose of regulating the business of insurance," would be plainly erroneous. Section 1363.1 would not meet the *Miller* two-part test because it does not "substantially affect the risk pooling arrangement between the insurer and the insured." *See Miller*, 123 S. Ct. at 1479.

REASONS FOR GRANTING THE WRIT

CERTIORARI SHOULD BE GRANTED TO RESOLVE CIRCUIT CONFLICTS OVER THE INTERPLAY BETWEEN THE MCCARRAN-FERGUSON ACT AND THE FEDERAL ARBITRATION ACT.

A. Certiorari is necessary to resolve the split among state and federal courts over whether the FAA preempts state laws that impose special requirements on arbitration agreements in healthcare or insurance plans.

1. The FAA policy in favor of enforcing arbitration agreements and the McCarran-Ferguson Act's goal of limiting federal control over insurance law collide when states impair arbitration clauses in insurance contracts.

The FAA provides that "[a] written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The FAA *preempts* state laws to the contrary under the Supremacy Clause of the United States Constitution. *See* U.S. Const. art. VI, cl. 2; *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 53-54 (1995).

The FAA is founded on a clear federal policy in favor of enforcing arbitration agreements. To implement that policy, the FAA preempts any state law that singles out an arbitration agreement for special treatment. Thus, the FAA provides that "[c]ourts may not . . . invalidate arbitration agreements under state laws applicable *only* to arbitration provisions." *Doctor's Assocs., Inc.*, 517 U.S. at 687.

In this past term, this Court reiterated its "presumption in favor of arbitration." *PacifiCare Health Sys., Inc. v. Book*, 123 S. Ct. 1531, 1536 n.2 (2003). This Court also held that the terms "'involving commerce'" in the FAA are "words of art that ordinarily signal the broadest permissible exercise of Congress' Commerce Clause power." *Citizens Bank v. Alafabco, Inc.*, 123 S. Ct. 2037, 2040 (2003). Thus, every effort should be made to interpret the scope of the FAA's preemption effect broadly.

The McCarran-Ferguson Act provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." 15 U.S.C. § 1012(b). The McCarran-Ferguson Act was passed to reaffirm that states have primary regulatory control over insurance. *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 40-41 (1996). In enacting the McCarran-Ferguson Act, "Congress was mainly concerned with the relationship between *insurance ratemaking* and the *antitrust laws*, and with the power of the States to tax insurance companies." *SEC v. Nat'l Sec.*, 393 U.S. 453, 458-59 (1969) (emphasis added). The purpose of the McCarran-Ferguson Act is "the avoidance of *'inadvertent* federal intrusion' into state insurance regulation," *Patenaude v. Equitable Life Assurance*, 290 F.3d 1020, 1026 (9th Cir. 2002), and it "is to be *'narrowly construed* in the face of valid federal regulatory interests.'" *Cochran v. Paco, Inc.*, 606 F.2d at 467 (emphasis added).

Because the FAA and the McCarran-Ferguson Act address fundamentally different concerns, there is no clear resolution when the acts intersect at the point where arbitration clauses appear in insurance contracts and states seek to impair those contractual clauses.

2. There is a split in authority on the question of whether and when the McCarran-Ferguson Act saves state laws affecting arbitration clauses from FAA preemption.

The question of whether the McCarran-Ferguson Act precludes FAA preemption of state laws that regulate arbitration agreements in insurance plans has been litigated extensively in the state and federal courts, with some courts holding that the FAA preempts such laws, and other courts holding that the McCarran-Ferguson Act saves those laws from FAA preemption. *See supra* pp. 6-7; *see also* Kristen Angus, *Tenth Circuit Surveys: Arbitration*, 76 DENV. U. L. REV. 681, 690-692 (1999) ("There is a split on this issue within the circuits and silence from the Supreme Court. The Second and Ninth Circuits have held that the McCarran-Ferguson Act does not preclude application of the FAA . . . The Tenth Circuit . . . joined the Fifth and Sixth Circuits in finding that state statutes regulating liquidation are protected from federal preemption by the Federal Arbitration Act.").

The Alabama Supreme Court undertook to determine whether the FAA preempted the combination of a general state law prohibiting the specific performance of any arbitration agreement and an insurance law subjecting any insurance contract to the general laws of the state. *Am. Bankers Ins. Co. of Fla.*, 757 So.2d at 1131-36. A party seeking to avoid arbitration under a clause in an insurance contract invoked the McCarran-Ferguson Act as a basis for saving Alabama's anti-arbitration statute from FAA preemption. The court held that the McCarran-Ferguson Act did not apply because Alabama's anti-arbitration provision "does not have the effect of 'transferring or spreading a policyholder's risk'" and thus is not a law regulating the business of insurance. *Id.* at 1133. Even though the state law "does impact the relationship

between the insurer and the insured, in that it governs the method of resolving disputes that arise between them, the impact is attenuated." *Id.*

Other courts have similarly addressed the application of state laws that impair enforcement of arbitration agreements in insurance contracts or prevent courts from being divested of jurisdiction to hear insurance contractual disputes. Some courts, like the Alabama Supreme Court in *American Bankers*, have found in those circumstances that the FAA preempts state law because such regulation of arbitration agreements does not constitute a regulation of the business of insurance. *E.g.*, *DiMercurio,* 202 F.3d at 75-81; *Hamilton Life Ins. Co. of N.Y.*, 408 F.2d at 610-11; *Bullock*, 165 F. Supp. 2d at 1261-62; *In re Arbitration of Mut. Reinsurance Bureau*, 750 F. Supp. at 459-62; *Towe, Hester & Erwin, Inc.*, 947 P.2d at 597-99.

However, other courts have found that the McCarran-Ferguson Act prevents FAA preemption of state laws in such circumstances. For example, the Eighth Circuit has held that a Missouri law providing for the enforcement of all contractual arbitration agreements except for those contained in insurance contracts is saved from FAA preemption because the Missouri law is a law that regulates the business of insurance. *Standard Sec. Life Ins. Co. of N.Y.*, 267 F.3d at 823-24; *see also In re Arbitration of Mut. Reinsurance Bureau*, 969 F.2d at 934-35; *Cont'l Ins. Co.*, 565 S.E.2d at 604; *Friday*, 939 P.2d at 872-73; *Cox,* 556 S.E.2d at 401-02. In this case, like the Eighth Circuit, the Court of Appeal held that the McCarran-Ferguson Act saves laws such as section 1363.1 from FAA preemption. App. 6-14.

As put by one of the commentators struck by the split among jurisdictions, "courts have reached differing conclusions over whether the McCarran-Ferguson Act precludes Federal Arbitration Act preemption." *See* Jennifer Nicole

Taylor, *Recent Development: Erickson v. Aetna Health Plans of California, Inc.: When the Federal Arbitration Act Closes One Courtroom Door, Let the McCarran-Ferguson Act Open Another*, 28 W. ST. U. L. REV. 257, 272-74 (2000); *see also* Willy E. Rice, *Federal Courts and the Regulation of the Insurance Industry: An Empirical and Historical Analysis of Courts' Ineffectual Attempts to Harmonize Federal Antitrust, Arbitration, and Insolvency Statutes with the McCarran-Ferguson Act – 1941-1993*, 43 CATH. U. L. REV. 399, 431-32 (1994). Another commentator, describing the split among the circuits, has noted that "Accepting certiorari on [*United States Dept. of the Treasury v. Fabe*, 508 U.S. 491 (1993)], the Supreme Court failed to define the relationship between the McCarran-Ferguson Act and the FAA. . . . This lack of direction from the Supreme Court has led to a split in the circuits on the question of whether the FAA applies to insurance contracts. The Tenth Circuit's decision marks a rare instance where other public policy concerns outweigh the presumption favoring arbitrability. [The Tenth Circuit's decision] further marks the rare instance where the presumption favoring arbitrability is overcome, not by a congressional command, but by judicial directive." Kristen Angus, *supra*, 76 DENV. U. L. REV. at 690-92.

Certiorari is appropriate to resolve the clear conflict among the courts on this recurring issue of intersecting federal policies.

B. Independent of the FAA-specific question presented in this case, certiorari is necessary to resolve various circuit splits over interpretation of the McCarran-Ferguson Act.

1. There is a circuit split over the determination of when a federal statute "specifically relates to the business of insurance."

a. This Court has not fully resolved the meaning of "specifically relates" as used in the McCarran-Ferguson Act.

A question raised by this petition is whether a federal law, such as the FAA and others, can be so clearly meant to preempt any contrary state law – including insurance laws – that preemption may apply notwithstanding the McCarran-Ferguson Act even if the text of the federal statute does not refer to insurance.

This court has only once addressed the meaning of the phrase "specifically relates" in the first clause of the McCarran-Ferguson Act, providing that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act *specifically relates to the business of insurance*." 15 U.S.C. § 1012(b) (emphasis added). In *Barnett Bank of Marion County, N.A.*, 517 U.S. 25, this court noted that "[t]he word 'relates' is highly general, and this Court has interpreted it broadly in other pre-emption contexts." *Id.* at 38. "'Specifically' can mean 'explicitly, particularly, [or] definitely.'" *Id.* Applying that definition, this court found that a law that "grants national banks permission to 'act as the agent for any fire, life, or other insurance company,' to 'solici[t] and sel[l] insurance'" *did* "specifically relate" to insurance. *Id.* at 39.

Barnett does not resolve the question implicated here, because the statute in *Barnett* involved a law that did refer to insurance in its text. *Barnett* left open the

question of whether there can be a federal law that is so clearly meant to apply to preempt all contrary state laws, including those relating to insurance, that it is irrelevant whether the law refers to insurance in its text.

b. Some courts have held that a federal law can preempt a state insurance law even if the federal law does not refer to insurance in its text.

Second Circuit: The Second Circuit has interpreted the McCarran-Ferguson Act quite narrowly on this point. In *Spirt v. Teachers Ins. & Annuity Ass'n*, the court determined that Title VII applied to an insurance company and preempted a contrary state law even though Title VII did not specifically provide that it was meant to apply to insurance. 691 F.2d 1054, 1065-66 (2d Cir. 1982), *vacated on other grounds*, *Teachers Ins. & Annuity Ass'n v. Spirt*, 463 U.S. 1223 (1983), *reinstated on other grounds*, *Spirt v. Teachers Ins. & Annuity Ass'n*, 735 F.2d 23 (2d Cir. 1984). The court relied on the "broad and explicit preemption provision" contained in Title VII and on the fact that "Title VII is not being *construed* to *implicitly* pre-empt state laws." *Spirt*, 691 F.2d at 1065.

In *Stephens v. National Distillers and Chemical Corp.*, 69 F.3d at 1231, the court was confronted with the question of whether the McCarran-Ferguson Act precluded the Foreign Sovereign Immunities Act (FSIA) from preempting a contrary state law. The court recognized that the *state* law in question regulated the business of insurance and that the FSIA did *not* refer to insurance in its text. *Id.* Nonetheless, the court held that the FSIA preempted the state law: "the McCarran-Ferguson Act does not preclude the preempting of New York's pre-judgment security requirement. The Supreme Court's language in *Fabe* in no

way compels such a broad reading of the McCarran-Ferguson Act, while prior case law in this Court, at the very least, recommends a narrower reading of the statute." *Id.* The court recognized that where a federal statute has a "'broad and explicit preemptive provision'" and "wherever federal law clearly intends to displace all state laws to the contrary," then the McCarran-Ferguson Act provides no bar to the federal law's application to insurance even if there is not a specific reference to insurance made in the text of the statute. *Id.* at 1232-33; *see also Bernstein*, 606 F. Supp. at 101 n.6 ("The Second Circuit has found that the lack of an explicit reference to insurance in a federal law does not automatically place it within the McCarran-Ferguson Act."). In *Stephens*, the Second Circuit also reaffirmed its pre-*Fabe* holding in *Spirt v. Teachers Ins. & Annuity Ass'n. See Stephens*, 69 F.3d at 1233.

The Second Circuit has also held that the Securities Litigation Uniform Standards Act of 1998 (SLUSA) is not reverse-preempted by the McCarran-Ferguson Act even though SLUSA does not refer to insurance in its text. *Lander v. Hartford Life & Annuity Ins. Co.*, 251 F.3d 101, 116-17 (2d Cir. 2001). In support of its holding, the court noted that "[i]t is only when a statute, by unintended implication, encroaches on the insurance regulatory regime of a state that McCarran-Ferguson prevents application of the federal statute. . . . But when the intended effect of a federal statute is to displace state regulations, we must give effect to this intent, regardless of whether an insurance company is involved." *Id.* The court also noted that "Congress passed SLUSA to provide uniform, national standards for litigation concerning a defined set of nationally marketed securities . . . – a topic undisputably of national concern." *Id.* at 117.

Eleventh Circuit: The Eleventh Circuit has acknowledged the Second Circuit's conclusion that the McCarran-Ferguson Act does not apply to a federal law that is clearly

meant to apply to insurance, even though it does not refer to insurance in its text: "[t]here has been some suggestion that the McCarran-Ferguson reverse preemption provisions should not apply in the context of the Bank Act, because the Bank Act was by its nature intended to preempt all conflicting state laws. In other contexts, federal laws involving issues of paramount national concern – such as the Foreign Sovereign Immunities Act (FSIA) and the Civil Rights Act of 1964 (Title VII) – have been held to be exempt from the reverse preemption provisions of McCarran-Ferguson." *Blackfeet Nat'l Bank*, 171 F.3d at 1244 n.10. The court ultimately found that the Bank Act did not rise to the level of national concern as did FSIA or Title VII, but did not explain at what point a national policy embodied in a federal law is sufficiently important so as to preempt state laws notwithstanding the McCarran-Ferguson Act. *Id.* at 1244.

Other courts: Other courts have also found that federal statutes can apply to preempt contrary state insurance laws *notwithstanding* their failure to specifically refer to insurance. *E.g.*, *Md. Cas. Co. v. Cushing*, 347 U.S. 409, 422 (1954) (Federal Maritime Law); *Sears, Roebuck & Co. v. All States Life Ins. Co.*, 246 F.2d 161, 172 (5th Cir. 1957) (Lanham Act).

c. Other courts, including the Court of Appeal here, have held that if the text of a federal law does not refer to insurance, then it cannot "specifically relate to insurance."

Seventh Circuit: The Seventh Circuit has directly challenged the Second Circuit's decision in *Spirt* and has offered a broader reading of the McCarran-Ferguson Act: "'No Act of Congress' could not be more comprehensive. The McCarran-Ferguson Act creates a rule of construction

applicable to all other federal laws, a 'plain statement' approach. . . . The second circuit [in *Spirt*] posed the wrong question when inquiring whether Congress meant to insulate the insurance business from civil rights laws. Congress did not tie its hands; instead it prescribed the consequences of silence and specificity in other acts past and future. . . . [F]ederal laws inconsistent with state laws apply when Congress says so directly." *NAACP*, 978 F.2d at 294-95. Consequently, the court held that Title VIII cannot preempt contrary state insurance laws because Title VIII does not specifically refer to insurance in its preemption provision. *Id.* at 295.

Fifth and Eighth Circuits: Other courts have also held that a federal statute that does not refer to insurance in its text cannot preempt any contrary state insurance laws because of the McCarran-Ferguson Act. *E.g.*, *Cochran*, 606 F.2d at 464 (Truth in Lending Act); *Murff*, 97 F.3d at 291 (Age Discrimination in Employment Act).

California: In the present case, the Court of Appeal rejected CHC's argument that the FAA is the type of federal statute that should preempt state insurance laws notwithstanding the fact that it does not refer to insurance in its text. App. 10-14. The issue appears to be one of first impression in California.

2. There is a circuit split over the effect *Fabe* had on the three-factor test set forth in *Royal Drug* and *Pireno* for non-antitrust cases.

a. This Court has not set forth a clear test for when state laws regulate the "business of insurance" in non-antitrust cases.

The McCarran-Ferguson Act has two clauses that make reference to the "business of insurance." The first clause, applicable to non-antitrust cases, provides that "[n]o Act of Congress shall be construed to invalidate,

impair, or supersede any law enacted by any State *for the purpose of regulating the business of insurance*." 15 U.S.C. § 1012(b) (emphasis added). The second clause, governing antitrust cases, provides that "the Act . . . known as the Sherman Act . . . and the Act . . . known as the Clayton Act, and the Act . . . known as the Federal Trade Commission Act . . . shall be applicable to the business of insurance to the extent that such business is not regulated by State law." *Id.*

This court grappled with the language of the first clause in *SEC v. Nat'l Sec., Inc.*, 393 U.S. 453, when it observed that "The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement – these were the core of the 'business of insurance.'" *Id.* at 460. However, this court did not set forth a specific test for determining what constitutes the " 'business of insurance.' "

This court subsequently formulated a three-factor test for determining whether a particular state statute regulates the " 'business of insurance' " under the second (or antitrust) clause of the McCarran-Ferguson Act. *E.g.*, *Pireno*, 458 U.S. at 129. Those factors are "*first*, whether the practice has the effect of transferring or spreading a policyholder's risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry." *Id.*; *see also Royal Drug Co.*, 440 U.S. 205. If the test is met, the state statute will not be preempted by any federal law except one that "specifically relates to the business of insurance."

After *Royal Drug* and *Pireno* it was unclear whether this three-factor test would also apply to the non-antitrust cases arising under the first clause of the McCarran-Ferguson Act. This court's decision in *United States Department of the Treasury v. Fabe*, 508 U.S. 491 did not

resolve the question. In *Fabe*, this court noted that both *Royal Drug* and *Pireno* "involved the scope of the antitrust immunity located in the *second* clause of § 2(b). We deal here with the *first* clause, which is not so narrowly circumscribed." *Id.* at 504. This court held that the first clause "necessarily encompasses more than" the second, or antitrust, clause because the first clause contains the additional language, "'enacted ... for the purpose of regulating the business of insurance.'" *Id.* at 504-05. However, this court did not expressly abrogate the use of the *Royal Drug/Pireno* three-factor test or set forth a clear new test to utilize in first clause cases.

This has led to confusion in the lower courts. Commentators have noted that, "[d]espite the Supreme Court's efforts, *Fabe* did not put an end to confusion over the definition of 'business of insurance.' After *Fabe's* analysis, the federal courts continue to struggle with 'business of insurance' cases. The question troubling lower courts in the wake of *Fabe* is whether they should completely disregard the *Pireno* test in first-clause [non antitrust] cases. Those lower courts that apply *Pireno* in the first-clause cases must also decide whether a broader application of 'business of insurance' is necessary outside the antitrust context. Various federal courts reached dissimilar answers to these questions." Peter B. Steffen, *After Fabe: Applying the Pireno Definition of 'Business of Insurance' in First-Clause McCarran-Ferguson Act Cases*, U. CHI. LEGAL F. 447, 463 (2000).

b. Some courts have held that *Fabe* precludes use of the *Royal Drug* and *Pireno* test in first clause cases.

Eighth Circuit: The Eighth Circuit has held that the three-factor *Royal Drug/Pireno test* has no place whatsoever in non-antitrust first clause cases: "the application of

the McCarran-Ferguson Act in this case does not require a specific conclusion that the allegedly improper activities of [defendant] constituted the 'business of insurance.' *Fabe* recognized that the three-part test of *Union Labor Life Ins. Co. v. Pireno* . . . for determining whether a particular practice constitutes the business of insurance is relevant only in cases involving a conflict between state law and federal antitrust law, a conflict which is the subject of a separate provision of the McCarran-Ferguson Act." *Norwest Bank Minn., N.A.*, 107 F.3d at 1305 n.8; *see also Owensboro National Bank*, 44 F.3d at 395 (Batchelder, J., dissenting) ("In light of *Fabe*, however, I believe that both the district court's and the majority's reliance on *Pireno* is misplaced.").

c. Other courts have held that the *Royal Drug* and *Pireno* three-factor test applies in first clause cases.

Ninth Circuit: The Ninth Circuit has held that the *Royal Drug* and *Pireno* test does apply to first clause non-antitrust cases: "[Defendant] argues that this three factor analysis should only be applied in the antitrust area, where the 'business of insurance' is meant to be defined narrowly. Hall contends that *United States Department of the Treasury v. Fabe* . . . supports this position. We disagree. In *Fabe*, the Supreme Court actually applied the three factors stated above, emphasizing that the acts involved there affected the transfer or spreading of risk. . . . On the other hand, [defendant] is correct that the Court held the business of insurance was to be defined more broadly outside the antitrust area. . . . This is a matter of degree, however, rather than a wholesale change in the inquiry." *Merchs. Home Delivery Serv., Inc.*, 50 F.3d at 1490 n.2.

Third, Sixth and Seventh Circuits: Other courts have also held that the *Royal Drug/Pireno* test applies to first clause, non-antitrust cases. *E.g.*, *Sabo*, 137 F.3d at 191 & n.3; *Owensboro Nat'l Bank*, 44 F.3d at 391-92; *Am. Deposit Corp.*, 84 F.3d at 840.

California: In the present case, the Court of Appeal adopted the reasoning in *Smith* and *Imbler*, which held that all the *Royal Drug/Pireno* factors "are merely '*considerations* to be weighed,'" in a first clause case like this one. *Smith*, 93 Cal. App. 4th at 159, 113 Cal. Rptr. 2d at 155; *see also Imbler*, 103 Cal. App. 4th at 575, 126 Cal. Rptr. 2d at 722; App. 9-10.

d. The circuits that apply the *Royal Drug* and *Pireno* test in non-antitrust first clause cases are split over how the test applies.

Even in those circuits that still utilize the *Royal Drug/Pireno* test in some manner for first clause cases, there is an additional split over the degree of utility that test retains in those cases. The split centers on the question of whether it is relevant that the defendant's conduct being challenged in the case actually constitutes the business of insurance, or whether McCarran-Ferguson reverse preemption is triggered so long as the particular state statute invoked by the plaintiff was intended to regulate the business of insurance.

Third Circuit: The Third Circuit has remarked on the circuit split: "We note at the outset that federal courts have seemingly disagreed as to the proper analytic inquiry into McCarran-Ferguson Act preclusion. . . . Some courts draw upon a four-part inquiry. . . . Other courts have announced a more truncated three-part test that does not require a specific conclusion that the defendant's conduct

constitutes the business of insurance." *Sabo*, 137 F.3d at 189 n.2.

Ninth Circuit: The Ninth Circuit employs a four-part inquiry to determine whether the McCarran-Ferguson Act precludes the preemption of a state insurance law by another federal statute in non-antitrust first clause cases: "(1) the [federal] statute does not 'specifically relate' to the business of insurance, (2) the acts challenged under the [state] statute constitute the business of insurance, (3) the state has enacted a law or laws regulating the challenged acts, and (4) the state law would be superseded, impaired or invalidated by the application of the federal statute." *Merchs. Home Delivery Serv., Inc.*, 50 F.3d at 1489. The important aspect of this approach is the second factor, which requires that defendant's conduct itself constitutes the business of insurance.

Seventh Circuit: The Seventh Circuit directly challenges the Ninth Circuit's requirement that the defendant's conduct itself constitute the business of insurance. Instead, the Seventh Circuit employs a three-part test that focuses on the purpose behind the state statute that is sought to be preempted: "first, does the federal statute at issue 'specifically relate to the business of insurance;' second, was the state statute 'enacted . . . for the purpose of regulating the business of insurance;' and third, would application of the federal statute 'invalidate, impair or supersede' the state law." *Autry*, 144 F.3d at 1040-41.[7]

[7] The first and third parts of the Seventh Circuit's test are identical to the first and fourth parts of the Ninth Circuit's test. The split in authority centers around the difference between the Seventh Circuit's second part of the test and the Ninth Circuit's second and third parts of the test.

The Seventh Circuit rejects the Ninth Circuit's four-part test because "[t]he four-part test requires the court to examine the activity at issue to determine whether the *activity being regulated* is part of the 'business of insurance.' However, the statutory language counsels us to examine the *purpose for which the statute was enacted* to determine whether the statute is one 'enacted . . . for the purpose of regulating the business of insurance.' While this distinction may seem somewhat semantic, the effect is far from inconsequential." *Id.* at 1041.

California: In the present case, the Court of Appeal adopted the reasoning in *Smith* and *Imbler*, which held that the relevant focus is on the statute's purpose in a first clause case like this one. *See Imbler*, 103 Cal. App. 4th at 574-75, 126 Cal. Rptr. 2d at 721; *Smith*, 93 Cal. App. 4th at 159-61, 113 Cal. Rptr. 2d at 155-56; *see also* App. 9-10.

3. This Court should grant certiorari to hold that the new two-part test set forth in *Kentucky Ass'n of Health Plans, Inc. v. Miller* applies in McCarran-Ferguson Act cases.

The same three-factor *Royal Drug/Pireno* test used in McCarran-Ferguson jurisprudence has also, until last term, been used in ERISA cases to determine whether a law is one "'which regulat[es] insurance' under [29 U.S.C.] § 1144(b)(2)(A)," and thus is saved from ERISA preemption. *Miller*, 123 S. Ct. at 1477. In *Miller*, this Court identified problems with the *Royal Drug/Pireno* three-factor test:

> Our holdings in *UNUM* [*Life Ins. Co. of America v. Ward*, 526 U.S. 358 (1999)] and *Rush Prudential* [*HMO, Inc. v. Moran*, 536 U.S. 355 (2002)] – that a state law may fail the first McCarran-Ferguson factor yet still be saved from pre-emption under § 1144(b)(2)(A) – raise more

> questions than they answer and provide wide opportunities for divergent outcomes. May a state law satisfy *any* two of the three McCarran-Ferguson factors and still fall under the savings clause? Just one? What happens if two of three factors are satisfied, but not "securely satisfied" or "clearly satisfied," as they were in *UNUM* and *Rush Prudential*? Further confusion arises from the question whether the *state law itself* or the *conduct regulated by that law* is the proper subject to which one applies the McCarran-Ferguson factors. In *Pilot Life*, we inquired whether Mississippi's *law of bad faith* has the effect of transferring or spreading risk, whether *that law* is integral to the insurer-insured relationship, and whether *that law* is limited to the insurance industry. *Rush Prudential*, by contrast, focused the McCarran-Ferguson inquiry on the *conduct regulated* by the state law, rather than the state law itself.

Id. at 1478 (citations omitted). This Court further noted that prior cases' analyses had "rendered the third McCarran-Ferguson factor a mere repetition of the prior inquiry into whether a state law is 'specifically directed toward' the insurance industry under the 'common-sense view.'" *Id.* at 1478 n.4.

Consequently, in *Miller* this Court held: "Today we make a clean break from the McCarran-Ferguson factors and hold that for a state law to be deemed a 'law . . . which regulates insurance' under [29 U.S.C.] § 1144(b)(2)(A), it must satisfy two requirements. First, the state law must be specifically directed toward entities engaged in insurance. . . . Second, as explained above, the state law must substantially affect the risk pooling arrangement between the insurer and the insured." *Miller*, 123 S. Ct. at 1479.

The same reasons given for modifying the three-factor McCarran-Ferguson Act test in the ERISA context apply

with equal force in the McCarran-Ferguson Act context. There is simply no workable test for determining the McCarran-Ferguson Act's effect when a court finds some, but not all, of the three factors defining the "business of insurance" are met. *E.g.*, *Am. Deposit Corp.*, 84 F.3d at 840 ("The first and most important factor in determining whether a practice is the 'business of insurance' is whether it spreads policyholder risk."); *Merchs. Home Delivery Serv., Inc.*, 50 F.3d at 1491 (absence of transfer or spread of risk factor "requires, at a minimum, that the other two factors weigh strongly in Hill's favor in order for the practice to fall within the business of insurance"); *Smith*, 93 Cal. App. 4th at 161, 113 Cal. Rptr. 2d at 156-57 (section 1363.1 "does not transfer risk" but other factors are met, so McCarran-Ferguson Act applies); *Imbler*, 103 Cal. App. 4th at 576, 126 Cal. Rptr. 2d at 722 (same). Thus, courts are also split on the question of the consequence for failing to meet the spreading risk factor of the *Royal Drug/Pireno* test.

This Court's new two-part test, in which *both* parts must be met, is simpler to apply and provides a bright-line distinction. It avoids the problem of what occurs if some, but not all, of the three *Royal Drug/Pireno* factors are met. It also goes to the heart of what the McCarran-Ferguson Act is designed to protect – states' right to regulate the core of insurance.

If the new *Miller* test were applied to the present case, section 1363.1 would plainly *not* be saved from preemption by McCarran-Ferguson because it is not a law that "substantially affect[s] the risk pooling arrangement between the insurer and the insured." *Miller*, 123 S. Ct. at 1477; *see Imbler*, 103 Cal. App. 4th at 576, 126 Cal. Rptr. 2d at 722-23 (holding that section 1363.1 is not a statute that transfers risk).

Although CHC asserted in a timely petition for rehearing that the Court of Appeal erred in failing to apply the new two-part test, the court denied rehearing, App. 24, and affirmed its adoption of the reasoning in *Smith* and *Imbler*, applying all the *Royal Drug/Pireno* factors and deciding that section 1363.1 is saved from FAA preemption. App. 6-14; *Imbler*, 103 Cal. App. 4th at 574-77, 126 Cal. Rptr. 2d at 721-22; *Smith*, 93 Cal. App. 4th at 159-62, 113 Cal. Rptr. 2d at 155-56.

CONCLUSION

This case involves numerous circuit splits over important issues regarding the interaction between the McCarran-Ferguson Act and the Federal Arbitration Act. Accordingly, certiorari is warranted. Moreover, the McCarran-Ferguson Act and the Federal Arbitration Act are both important federal statutes which are frequent subjects of litigation in state and federal courts. The intersection of these two important federal statutes has caused tremendous difficulty in the lower courts, and it is incumbent on this Court to provide guidance to the lower courts on the questions presented by this petition.

Respectfully submitted,

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NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

California Rules of Court, rule 977(a), prohibits courts and parties from citing or relying on opinions not certified for publication or ordered published, except as specified by rule 977(b). This opinion has not been certified for publication or ordered published for purposes of rule 977.

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION FOUR

MUZEYYEN BALABAN-ZILKE, individually, etc., Plaintiff and Respondent, v. CIGNA HEALTHCARE OF CALIFORNIA, INC., et al., Defendants and Appellants.	B140672 (Los Angeles County Super. Ct. No. BC209255) (Filed May 28, 2003)

APPEALS from orders of the Superior Court of Los Angeles County, Irving S. Feffer, Judge. Affirmed.

Horvitz & Levy, Lisa Perrochet, John A. Taylor, Jr., Sandra J. Smith, Jeremy B. Rosen; Pivo, Halbreich, Cahill & Yim, Richard F. Cahill and Eva S. Halbreich for Defendant and Appellant Cigna Healthcare of California, Inc.

Marrone, Robinson, Frederick & Foster, J. Alan Frederick and Ilona Gordon for Defendants and Appellants Medipace Medical Group, Inc., and Victor Gura, M.D.

Mazursky, Schwartz & Angelo, Christopher E. Angelo; Angelo & DiMonda; Mazursky & Schwartz; Kornarens & Howard, Anthony Kornarens, and Edward P. Howard for Plaintiff and Respondent.

Appellants in these consolidated appeals challenge the denial of their respective petitions to compel arbitration. We affirm.

FACTUAL AND PROCEDURAL BACKGROUND

On April 23, 1999, respondent Muzeyyen Balaban-Zilke, proceeding as an individual and as successor-in-interest to Brad Zilke, initiated the underlying action against appellants CIGNA Healthcare of California, Inc. (CHC), Medipace Medical Group, Inc., and Victor Gura, M.D. Balaban-Zilke's first amended complaint asserted claims for breach of contract, breach of the implied covenant of good faith and fair dealing, violations of the Consumers Legal Remedies Act (Civ. Code, § 1750 et seq.), intentional infliction of emotional distress, negligent and intentional misrepresentation, unfair business practices (Bus. & Prof. Code, § 17200 et seq.), corporate negligence, breach of fiduciary duty, and wrongful death.

The first amended complaint alleged the following facts: Since 1992, Balaban-Zilke had obtained medical insurance for herself and her husband, Brad Zilke, through a group plan offered by her employer, the County of Los Angeles (County). Balaban-Zilke selected a CHC health plan over other choices on the basis of CHC's representations regarding the quality of medical care that it provided.

The complaint further alleges that in November 1996, Dr. Gura, who is Medipace's medical director and a CHC "gatekeeper," removed a cancerous mole from Brad Zilke's back. Although a pathology report indicated that the cancer had infiltrated Brad Zilke's lymphatic system, Dr. Gura stated that he was cancer free and denied his request to see a specialist. Brad Zilke successfully appealed this denial to CHC, and a specialist recommended that he should receive a full body CT scan and full laboratory studies. Upon hearing the recommendations, Dr. Gura responded that Balaban-Zilke had "cheap insurance. . . . " Without informing Brad Zilke, he ordered only a partial CT scan, which indicated that Brad Zilke was cancer free. Brad Zilke died of cancer in November 1998.

On October 4, 1999, CHC filed a motion and petition to compel arbitration, citing an arbitration provision in the group service agreement between CHC and the County. Subsequently, Medipace and Dr. Gura filed a motion and a petition to compel arbitration on January 5, 2000. They contended that they were entitled to arbitration as third party beneficiaries of the arbitration provision in the group service agreement, and under a separate physician-patient arbitration agreement signed by Brad Zilke.

On January 25, 2000, the trial court denied the motions and petitions to compel arbitration.[1] On February 25, 2000, CHC filed a motion for reconsideration, in which

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[1] Balaban-Zilke subsequently filed a second amended complaint, which reasserts her claims in the first amended complaint, and does not differ from her first amended complaint in any way material to the issues before us in this appeal.

Medipace and Dr. Gura attempted to join. The trial court denied this motion on April 3, 2000.

CHC, Medipace, and Dr. Gura noticed an appeal (B140672) from the orders denying their respective motions and petitions to compel arbitration and motion for reconsideration, and CHC noticed an appeal (B142412) from the order denying its motion for reconsideration. These appeals were subsequently consolidated. On December 26, 2000, we granted CHC's petition for writ of supersedeas (B140672), and issued a writ of supersedeas staying proceedings before the trial court.

DISCUSSION

I.

CHC contends that the trial court erred in denying its request to compel arbitration and motion for reconsideration. It is mistaken.

A. *Petition to Compel*

The trial court may deny a petition to compel arbitration if it determines that "[g]rounds exist for the revocation of the agreement." (Code Civ. Proc., § 1281.2.) Here, the trial court declined to enforce the arbitration provision of the group service agreement on numerous grounds, including that CHC failed to comply with Health and Safety Code section 1363.1 (section 1363.1), a provision of the Knox-Keene Health Care Service Plan Act (Knox-Keene Act) (Health & Saf. Code, § 1340 et seq.). Because

we conclude that the trial court ruled correctly on this matter, we do not address CHC's other contentions regarding the petition to compel arbitration.[2]

"In California, health care service plans (or HMO's) are licensed and regulated by the Department of Managed Care under the Knox-Keene Act." (*Smith v. PacifiCare Behavioral Health of Cal., Inc.* (2001) 93 Cal.App.4th 139, 150, fn. omitted.) Section 1363.1 of that act "provides that a binding arbitration clause in a health care service plan must incorporate various disclosures, including a clear statement of 'whether the subscriber or enrollee is waiving his or her right to a jury trial. . . . ' The waiver language . . . must appear immediately before the signature line for the individual enrolling in the plan. [Citation.]"[3] (*Erickson*

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[2] We also do not address alternative grounds for affirming the ruling, including those that were first presented by Balaban-Zilke's counsel following the completion of briefing, and that rely on purported facts outside the record. (*Filipino Accountants' Assn. v.. State Bd. of Accountancy* (1984) 155 Cal.App.3d 1023, 1029.)

[3] Section 1363.1 states: "Any health care service plan that includes terms that require binding arbitration to settle disputes and that restrict, or provide for a waiver of, the right to a jury trial shall include, in clear and understandable language, a disclosure that meets all of the following conditions: [¶] (a) The disclosure shall clearly state whether the plan uses binding arbitration to settle disputes, including specifically whether the plan uses binding arbitration to settle claims of medical malpractice. [¶] (b) The disclosure shall appear as a separate article in the agreement issued to the employer group or individual subscriber and shall be prominently displayed on the enrollment form signed by each subscriber or enrollee. [¶] (c) The disclosure shall clearly state whether the subscriber or enrollee is waiving his or her right to a jury trial for medical malpractice, other disputes relating to the delivery of service under the plan, or both, and shall be substantially expressed in the wording provided in subdivision (a) of Section 1295 of the Code of Civil Procedure. [¶] (d) In any contract or enrollment agreement for a health care service plan, the disclosure required by this

(Continued on following page)

v. Aetna Health Plans of California, Inc. (1999) 71 Cal.App.4th 646, 650.)

Here, CHC's petition to compel arbitration is unsupported by evidence that it made the disclosures required by section 1363.1. In opposition to the petition, Balaban-Zilke pointed out that the group services agreement attached to the petition identifies the Knox-Keene Act as law applicable to the agreement and incorporates its terms. She also submitted a declaration stating that she never saw or signed an enrollment form disclosing the arbitration provision, and thus she was not in a position to object to the provision or to enroll in another plan.

The record thus unequivocally supports the trial court's finding that CHC had not complied with section 1363.1. To explain why this finding is dispositive, we recount the emerging law regarding section 1363.1 in the context of the briefing in this appeal.

CHC's opening brief contends that section 1363.1 is preempted by the Federal Arbitration Act (FAA) (9 U.S.C. § 1 et seq.), citing *Erickson v. Aetna Health Plans of California, Inc., supra,* 71 Cal.App.4th 646. In *Erickson,* an insured sued an HMO, alleging that it had not provided the insured with timely cancer treatment. (*Id.* at p. 649.) The trial court denied the HMO's motion to compel arbitration, reasoning that the arbitration provision in the

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section shall be displayed immediately before the signature line provided for the representative of the group contracting with a health care service plan and immediately before the signature line provided for the individual enrolling in the health care service plan."

pertinent agreement with the insured did not comply with section 1363.1.

Division Two of the Fourth Appellate District reversed, holding that the FAA preempts section 1363.1. With exceptions not relevant here (9 U.S.C. § 1), the FAA provides that an arbitration clause in a "contract evidencing a transaction involving commerce" is enforceable, "*save* upon such grounds as exist at law or in equity for the revocation of *any* contract." (9 U.S.C. § 2, italics added; *Erickson v. Aetna Health Plans of California, Inc., supra,* 71 Cal.App.4th at p. 650.) Because section 1363.1 imposes a special disclosure requirement on health care arbitration clauses, the *Erickson* court reasoned that it was displaced by the FAA, which permits courts to deny enforcement of arbitration provisions solely on the basis of "'generally applicable contract defenses. . . . '" (*Erickson,* at pp. 650-652, quoting *Doctor's Associates, Inc. v. Casarotto* (1996) 517 U.S. 681, 687.)

However, after the completion of briefing in the appeals before us, Division Three of the Second Appellate District reached a contrary conclusion on essentially similar facts in *Smith v. PacifiCare Behavioral Health of Cal., Inc., supra,* 93 Cal.App.4th 139. The court in *Smith* declined to follow *Erickson,* reasoning that the FAA cannot preempt section 1363.1 because of the operation of the McCarran-Ferguson Act (McCarran-Ferguson) (15 U.S.C. § 1011 et seq.). (*Smith,* at pp. 152-163.)

McCarran-Ferguson provides in pertinent part that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless

such Act specifically relates to the business of insurance. . . . " (15 U.S.C. § 1012(b).) From this general rule, McCarran-Ferguson exempts federal antitrust legislation as "applicable to the business of insurance to the extent that such business is not regulated by State Law." (15 U.S.C. § 1012(b).)

As the court explained in *Smith,* Congress enacted McCarran-Ferguson in 1945 in response to *U.S. v. South-Eastern Underwriters Assn.* (1944) 322 U.S. 533 (*South-Eastern Underwriters*), "which held that the business of insurance was 'commerce' within the meaning of the commerce clause and therefore the business of insurance was subject to all federal laws, including those relating to antitrust. [Citation.] This was a major change in the law. . . . [¶] The clear purpose of McCarran-Ferguson was to abrogate this change and to ensure that the states would continue to enjoy broad authority in regulating the dealings between insurers and their policyholders. [Citation.]" (*Smith v. PacifiCare Behavioral Health of Cal., Inc., supra,* 93 Cal.App.4th at p. 153.)

The court in *Smith* concluded that McCarran-Ferguson bars the preemption of section 1363.1 by the FAA, reasoning that the FAA is a statute of general application, HMO's regulated under the Knox-Keene Act are engaged in the business of insurance, and section 1363.1 was "enacted . . . for the purpose of regulating the business of insurance. . . . " (15 U.S.C. § 1012(b).) In determining that section 1363.1 regulates the business of insurance, the *Smith* court applied a three-factor test found in *Union Labor Life Ins. Co. v. Pireno* (1982) 458 U.S. 119, 129, as well as other criteria used by the United States Supreme Court.

CHC submitted supplemental briefing regarding *Smith,* contending that *Erickson,* rather than *Smith,* had properly assessed whether the FAA preempts section 1363.1. However, after the completion of supplemental briefing, a panel of justices from Division Two of the Fourth Appellate District – including the justice who had written the opinion in *Erickson* – followed *Smith* in *Imbler v. PacifiCare of Cal., Inc.* (2002) 103 Cal.App.4th 567.[4]

As in the case before us, the trial court in *Imbler* denied an HMO's petition to compel arbitration for failure to comply with section 1363.1. (*Imbler v. PacifiCare of Cal., Inc., supra,* 103 Cal.App.4th at pp. 568-569.) Noting that *Erickson* did not address McCarran-Ferguson, the *Imbler* court examined *Smith* at length, including its application of the *Pireno* test, and concluded that *Smith* had properly determined that the FAA does not preempt section 1363.1. (*Imbler,* at pp. 569-579.) The *Imbler* court thus affirmed the denial of the petition to compel arbitration. (*Ibid.*)

In view of *Smith* and *Imbler,* the trial court in the case before us also correctly denied CHC's petition to compel arbitration. CHC nonetheless urges us to reject *Smith* on three grounds, contending: (1) *Smith* misapplied the *Pireno* test; (2) HMO's regulated by the Knox-Keene Act are not "insurance" within the meaning of McCarran-Ferguson; and (3) *Smith* thwarts the federal policy in favor of enforcing the FAA. However, given the careful demonstrations in *Smith* and *Imbler* that section 1363.1

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[4] With prior notice, we provided the parties an opportunity to address *Imbler* during oral argument.

regulates the business of insurance under the *Pireno* test and other applicable criteria, we decline to revisit this issue. Accordingly, we limit our attention to contentions (2) and (3), which are not fully addressed in *Smith.*

CHC contends that it is not engaged in the business of insurance under McCarran-Ferguson, arguing that when Congress enacted this legislation, health care plans, as then incarnated, were not viewed as insurance. We are not persuaded. The United States Supreme Court has cautioned that the reach of McCarran-Ferguson cannot be elicited simply by "a detailed point-by-point comparison between the regime created by McCarran-Ferguson and the one that existed before." (*Department of Treasury v. Fabe* (1993) 508 U.S. 491, 508.) Moreover, after *Smith* issued, the Supreme Court stated that an HMO "provides health care, and it does so as an insurer." (*Rush Prudential HMO, Inc. v. Moran* (2002) 536 U.S. 355, 367, reversed on another ground in *Kentucky Assn. of Health Plans, Inc. v. Miller* (2003) ___ U.S. ___ [123 S.Ct. 1471, 1479].) Although this determination occurs in a discussion of preemption of state law by the Employee Retirement Income Security Act of 1974 (ERISA) (29 U.S.C. § 1001 et seq.), it supports *Smith,* as the court in *Imbler* observed. (*Imbler v. PacifiCare of Cal., Inc., supra,* 103 Cal.App.4th at p. 574.)

CHC also contends that Congress intended the FAA to displace state laws such as section 1363.1 despite McCarran-Ferguson, pointing to the strong federal policy favoring arbitration. It cites four cases in which federal laws of general application were held to preempt state insurance regulations, notwithstanding McCarran-Ferguson.

We agree that the FAA evidences a strong policy in favor of arbitration. However, the cases cited by CHC do not indicate that such a policy, by itself, places a federal law of general application outside the reach of McCarran-Ferguson. In each case, the court identified factual circumstances that nullified the operation of McCarran-Ferguson. As we explain below, these circumstances are not present in the case before us.

In three of the cases that CHC cites, the courts determined that McCarran-Ferguson was inapplicable because the state regulation invaded matters subject to federal authority or law before *South-Eastern Underwriters.* In *Maryland Cas. Co. v. Cushing* (1954) 347 U.S. 409, 413-414, the United States Supreme Court held that federal maritime laws displaced a state law permitting lawsuits against a maritime insurer, reasoning that McCarran-Ferguson did not permit states to regulate maritime litigation, over which they had lacked authority prior to *South-Eastern Underwriters.*

Subsequently, in *Sears, Roebuck & Co. v. All States Life Insurance Co.* (5th Cir. 1957) 246 F.2d 161, the court affirmed a determination that an insurer's corporate name did not violate the Lanham Act (15 U.S.C. § 1522 et seq.), which was enacted in 1946 to correct and enhance federal trademark legislation originating in 1905 (*Pacific Supply Coop. v. Farmers Union Central Exch., Inc.* (9th Cir. 1963) 318 F.2d 894, 905-906). Citing *Maryland Cas. Co.,* the *Sears, Roebuck* court stated in dicta that McCarran-Ferguson did not bar the Lanham Act claim at issue, notwithstanding the existence of a state regulation empowering a state board to approve insurer's names.

In *Stephens v. National Distillers and Chemical Corp.* (2d Cir. 1995) 69 F.3d 1226, 1233-1234, the court applied a similar rationale regarding the Federal Sovereign Immunities Act (FSIA). It concluded that the FSIA preempted the imposition of a state insurance regulation on foreign companies, despite McCarran-Ferguson, because the FSIA largely codified international and federal law in existence before McCarran-Ferguson.

In our view, the case before us falls outside *Maryland Cas. Co.* and its progeny because the states were at liberty to regulate arbitration clauses in insurance contracts prior to *South-Eastern Underwriters.* As the Supreme Court explained in *SEC v. National Securities, Inc.* (1969) 393 U.S. 453, 459, before *South-Eastern Underwriters* was decided in 1944, states "had a free hand in regulating the dealings between insurers and their policyholders. Their negotiations, and the contract which resulted, were *not considered commerce* and were, therefore, left to state regulation." (Italics added.) Thus, in enacting the McCarran-Ferguson Act, Congress intended to permit state regulation regarding "the 'business of insurance,'" a realm "that centers around the contract of insurance. . . . " (*Id.* at p. 460.) According to the court in *SEC,* "[t]he relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and *enforcement* – these were the core of the 'business of insurance.'" (*Ibid.,* italics added.)

The FAA, as enacted in 1925 and in its present form, is limited by its own terms to arbitration clauses in pertinent contracts "evidencing a transaction involving commerce" (9 U.S.C. § 2; see *Prima Paint v. Conklin* (1967) 388 U.S. 395, 397, 400-405). Although no court expressly addressed whether the FAA governed arbitration clauses

in insurance contracts before *South-Eastern Underwriters,* the legal principles in effect during that period, as described in *SEC,* exempted such clauses from the scope of the FAA. Furthermore, in 1931, the United States Supreme Court held that the Fourteenth Amendment to the United States Constitution did not bar states from mandating the inclusion of an arbitration provision in insurance contracts, reasoning that "the procedure by which rights may be enforced and wrongs remedied is peculiarly a subject of state regulation and control." (*Hardware Co. v. Glidden Co.* (1931) 284 U.S. 151, 158.) Accordingly, the rationale in *Maryland Cas. Co.* and its progeny does not apply here.

The fourth case cited by CHC is *Spirt v. Teachers Ins. & Annuity Assn.* (2d Cir. 1982) 691 F.2d 1054, certiorari granted and judgment vacated and remanded on other grounds by *Long Island University v. Spirt* (1983) 463 U.S. 1223, reinstated as modified on other grounds by (2d Cir. 1984) 735 F.2d 23. In *Spirt,* the court concluded that McCarran-Ferguson did not displace title VII of the Civil Rights Act of 1964 (title VII) (42 U.S.C. § 2000e et seq.) after examining their respective legislative histories. (*Spirt v. Teachers Ins. & Annuity Assn., supra,* 691 F.2d at pp. 1064-1066.) The *Sprit* [sic] court placed special emphasis on the express language of the preemption clause in title VII (42 U.S.C. § 2000e-7), which it believed indicated Congress's intent to impose requirements on the activities of insurers that could be classified as "the business of insurance" under McCarran-Ferguson. (*Spirt,* at pp. 1064-1066.)

Unlike the preemption clause in title VII, the analogous clause in the FAA limits it to relevant contracts "evidencing a transaction involving commerce" (9 U.S.C.

§ 2). However, as we have explained, Congress originally enacted this clause prior to *South-Eastern Underwriters,* when insurance contracts were deemed *not* to be "commerce." These historical facts distinguish the case before us from *Spirt.*

Finally, CHC advances two grounds for enforcing the arbitration clause, regardless of whether CHC violated section 1363.1. First, CHC argues that denying enforcement due to noncompliance with the special requirements in section 1363.1 conflicts with section 1281 of the Code of Civil Procedure, which provides that an arbitration agreement is unenforceable only "upon such grounds as exist for the revocation of *any* contract." (Italics added.) We are not persuaded.

"A proceeding to compel arbitration is in essence a suit in equity to compel specific performance of a contract. (*Freeman v. State Farm Mut. Auto. Ins. Co.* (1975) 14 Cal.3d 473. . . .) Accordingly, equitable principles come into play and the actions of a party seeking to compel arbitration can be considered by the trial court and this court. Specifically, no one can take advantage of his own wrong. (Civ. Code, § 3517.)" (*Weisman v. Johnson* (1982) 133 Cal.App.3d 289, 295.) Thus, to invoke equitable principles to enforce the arbitration provision, CHC must have "clean hands." (See *Gavina v. Smith* (1944) 25 Cal.2d 501, 505-506.)

The defense of unclean hands is generally available in equity. (11 Witkin, Summary of Cal. Law (9th ed. 1990) Equity, § 8, pp. 684-685.) Furthermore, as our Supreme Court remarked in *Gavina v. Smith, supra,* 25 Cal.2d at page 506, under the clean hands doctrine, "[o]ne who violates his contract cannot have recourse to equity to

support that very violation." Here, the disclosure requirements of section 1363.1 were incorporated into the group agreement by law (*City of Torrance v. Workers' Comp. Appeals Bd.* (1982) 32 Cal.3d 371, 378; 1 Witkin, Summary of Cal. Law (9th ed. 1987) Contracts, § 692, p. 625) and under the terms of the group agreement itself. In view of CHC's failure to make the requisite disclosures and Balaban-Zilke's consequent ignorance of the arbitration provision in selecting her health care provider, the trial court could have properly concluded that it was inequitable to enforce this provision. (See *Lawrence v. Walzer & Gabrielson* (1989) 207 Cal.App.3d 1501, 1504-1508.)

Second, CHC argues that the arbitration clause binds Balaban-Zilke because she accepted benefits under the group agreement, citing *NORCAL Mutual Ins. Co. v. Newton* (2000) 84 Cal.App.4th 64, 72-84, and *Avina v. Cigna Healthplans of California* (1989) 211 Cal.App.3d 1, 3. However, the holdings in these cases rely on the equitable principle that "[a] voluntary acceptance of the benefit of a transaction is equivalent to a consent to all the obligations arising from it, so far as the facts are known, or ought to be known, to the person accepting" (Civ. Code, § 1589). As we have explained, CHC may not invoke equitable principles to enforce the arbitration provision.

In sum, the trial court properly denied CHC's petition to compel arbitration upon finding that CHC had not complied with section 1363.1.

B. *Motion for Reconsideration*

CHC contends that the trial court erred in denying its motion for reconsideration, arguing that it submitted

evidence sufficient to establish that CHC had complied with section 1363.1.

Under Code of Civil Procedure section 1008, a party seeking reconsideration of a prior ruling upon an alleged different set of facts must "provide both newly discovered evidence and an explanation for the failure to have produced such evidence earlier. [Citation.]" (*Robbins v. Los Angeles Unified School Dist.* (1992) 3 Cal.App.4th 313, 317.) A ruling on a motion for reconsideration is reviewed for abuse of discretion. (*Glade v. Glade* (1995) 38 Cal.App.4th 1441, 1457.)

Here, CHC supported its motion for reconsideration with declarations from County employees responsible for employee insurance benefits, together with an unsigned enrollment form of a kind used in 1992, when Balaban-Zilke first applied for coverage, and an unsigned domestic partners enrollment form of a kind used in 1996, after the County extended health care benefits to domestic partners in 1995. According to the declarations, Brad Zilke could not have obtained coverage after 1996 unless he and Balaban-Zilke signed the domestic partners form, which discloses the arbitration clause immediately above the signature blocks.

The trial court denied the motion for reconsideration, concluding that (1) CHC had failed to explain the tardy production of this evidence, and that (2) the new evidence did not disturb its prior findings. We do not discern an abuse of discretion.

To begin, CHC did not offer a credible explanation for its failure to submit this evidence prior to January 25, 2000, when the trial court denied CHC's petition to compel arbitration. Shortly after CHC filed its petition on October

4, 1999, counsel for Balaban-Zilke pointed out in correspondence with CHC's counsel that the petition lacked evidence that CHC had complied with section 1363.1.

CHC's counsel denied that section 1363.1 was applicable, but agreed to continue the hearing on the petition. On or about October 15, 1999, CHC and Balaban-Zilke stipulated to a three-month continuance pending the decision in *Broughton v. Cigna Healthplans* (1999) 21 Cal.4th 1066, which was expected to resolve issues regarding the arbitrability of certain claims for injunctive relief asserted by Balaban-Zilke. The stipulation recites that CHC also wished to continue the hearing because it was conducting "a diligent search into further documentation to support its petition." However, CHC never submitted any evidence that it made the disclosures required under section 1363.1.

In connection with the motion for reconsideration, CHC submitted declarations stating that CHC could not provide a copy of the enrollment form signed by Balaban-Zilke in 1992 because the original had been destroyed after five years, in accordance with County policy. The declarations also stated that the domestic partners form signed by Brad Zilke in 1996 could not be released absent his representative's authorization. Finally, regarding the delay in submitting unsigned copies of the enrollment forms, CHC's declarations indicated that the kind of enrollment forms that Balaban-Zilke and Brad Zilke would have signed were not determined until February 2000, when CHC obtained copies of the pertinent group agreements from the County.

Although these declarations offer an explanation of CHC's inability to supply a copy of the 1992 enrollment

form signed by Balaban-Zilke, they are silent about CHC's failure to secure authorization to release the 1996 form signed by Brad Zilke and Balaban-Zilke, and its four-month delay in obtaining the underlying group agreements. Accordingly, the trial court did not err in concluding that CHC's tardy submission of evidence was not adequately explained.

However, assuming otherwise, the declarations and other materials submitted by CHC merely create a conflict in the evidence, given Balaban-Zilke's declaration that she never saw or signed an enrollment form that disclosed the arbitration clause. Because substantial evidence supports the determination that CHC violated section 1363.1, the trial court properly denied the motion for reconsideration. (*Shadow Traffic Network v. Superior Court* (1994) 24 Cal.App.4th 1067, 1083-1084.)

II.

Medipace and Dr. Gura also contend that the trial court erred in denying their petition to compel arbitration. We disagree.

The trial court denied this petition on several grounds, including that it was necessary to resolve Balalan-Zilke's claims against Medipace and Dr. Gura in the court action to avoid the danger of conflicting rulings (Code Civ. Proc., § 1281.2, subd.(c)). Because the trial court's ruling is properly affirmed on this basis, it is unnecessary to resolve Medipace and Dr. Gura's other contentions.

Subparts (1) and (4) of Code of Civil Procedure section 1281.2, subdivision (c), permit a trial court to "refuse to

enforce the arbitration agreement" or "stay arbitration pending the outcome of the court action" if it determines that "[a] party to the arbitration agreement is also a party to a pending court action or special proceeding with a third party, arising out of the same transaction or series of related transactions and there is a possibility of conflicting rulings on a common issue of law or fact." Rulings on these matters are consigned to the trial court's discretion. (*Henry v. Alcove Investment, Inc.* (1991) 233 Cal.App.3d 94, 101.)

As we have explained (see pt. I.A., *ante*), the trial court correctly denied CHC's petition to compel arbitration. Furthermore, the trial court determined that Balaban-Zilke's claim for unfair business practices (Bus. & Prof. Code, § 17200) against CHC, Medipace, and Dr. Gura, which Balaban-Zilke asserts on behalf of herself and the general public, is nonarbitrable under *Broughton v. Cigna Healthplans, supra,* 21 Cal.4th 1066. This ruling was correct, insofar as Balaban-Zilke seeks injunctive relief. (*Cruz v. Pacificare Health Systems, Inc.* (2003) 30 Cal.4th 303, 316.) [5]

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[5] Medipace and Dr. Gura contend that they are not proper parties to the unfair business practices claim because it rests on alleged misrepresentations solely by CHC. We decline to find error on this basis.

Joint liability for unfair business practices may rest on a theory of conspiracy. (*Saunders v. Superior Court* (1994) 27 Cal.App.4th 832, 845-846.) Here, Balaban-Zilke's first and second amended complaints allege that Medipace and Dr. Gura were *co-conspirators* in CHC's alleged misconduct. In addition, they allege, inter alia, that Dr. Gura was a consulting doctor employed by CHC and Medipace, that Dr. Gura acted as "gatekeeper" for CHC, and that Dr. Gura was Medipace's medical

(Continued on following page)

In view of these rulings, as well as the numerous claims that Balaban-Zilke alleges against all appellants,[6] the trial court could properly deny arbitration to avoid the possibility of conflicting rulings. Medipace and Dr. Gura nonetheless disagree, contending in conclusory terms that the trial court made no ruling on this matter. They are mistaken.

In opposing appellants' requests for arbitration, Balaban-Zilke asked the trial court to order joinder of arbitrable claims with the claims at issue in the court action, or to stay arbitration pending the outcome of the court action. She pointed to the nonarbitrable unfair business practices claim, and cited *Mercury Ins. Group v. Superior Court* (1998) 19 Cal.4th 332, 348, for the proposition that the right to arbitration may yield "if there is an

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director. Medipace and Dr. Gura do not argue that these allegations are insufficient to plead a conspiracy.

As Witkin explains: "The allegation of a conspiracy . . . serves a purpose. If the plaintiff seeks to hold several defendants liable for a tort as joint tortfeasors, he must prove that each in some way participated in the wrong. If he can show that each committed a wrongful act or some part of it, e.g., that each made false representations, he has no need of averments of conspiracy. But if A alone made representations, the plaintiff can hold B and C liable with A only by alleging and proving that A acted under an agreement (conspiracy) with B and C to defraud." (5 Witkin, Cal. Procedure (4th ed. 1997) Pleading, § 875, pp. 333-334.)

[6] Balaban-Zilke's first amended complaint (which was operative when the trial court ruled on the petitions to compel arbitration) and her second amended complaint (which was operative when the trial court ruled on the motion for reconsideration) each assert: (1) claims of breach of contract, intentional infliction of emotional distress, negligent and intentional misrepresentation, unfair business practices, and breach of fiduciary duty against CHC, Medipace, and Dr. Gura; and (2) a claim for corporate negligence against CHC and Medipace.

issue of law or fact common to the arbitration and a pending action or proceeding with a third party and there is a possibility of conflicting rulings thereon."

At the hearing on appellants' requests for arbitration on January 25, 2000, the trial court directed Balaban-Zilke's counsel to prepare orders denying these requests. The trial court signed the orders, as submitted, on February 10, 2000. Each order cited numerous grounds for denying the respective requests for arbitration. Furthermore, the order denying Medipace and Dr. Gura's request relies on the grounds cited in the order denying CHC's request, insofar as Medipace and Dr. Gura sought arbitration as third party beneficiaries of CHC's arbitration agreement.

Although neither order expressly mentions the need to avoid conflicting rulings, each order expressly bases the denial of arbitration on *all* the arguments that Balaban-Zilke had raised against arbitration. The order denying Medipace and Dr. Gura's request states: "The Court further adopts each of the other arguments made by [Balaban-Zilke] in [her] Opposition as a basis for its ruling." The order denying CHC's request contains a similar statement.

Appellants subsequently objected that the written orders did not accurately reflect the trial court's oral rulings. At the hearing on CHC's motion for reconsideration – in which Medipace and Dr. Gura attempted to join – the trial court heard oral argument on these objections. Counsel for Medipace and Dr. Gura contended that the written order denying their request for arbitration cited grounds that were not argued during the hearing on that request.

In addressing the motion for reconsideration and the objections to the written orders, the trial court observed that it could "split" the issues in the court action and arbitration. It remarked: "But nevertheless, I'm also aware of the fact that that is impractical in some instances, because you could get conflicting results. And in this case, that could very well happen. So that enters my thought process, that I don't like the splitting but I am aware of the fact that it's allowed, so I am just simply saying I don't particularly like it, so that – that's entered my thought process, I must confess."

The trial court then stated: "I think my order is consistent with my thought process of what I was doing. *I'm not going to change my order.*"[7] (Italics added.)

The trial court denied the motion for reconsideration, citing the lack of compliance with Code of Civil Procedure section 1008. It added: "[E]ven assuming that we were procedurally properly here, . . . I decline to [order arbitration] for *all the reasons that I said in my original order.* I don't think this is a proper case to compel arbitration." (Italics added.)

In view of this record, the February 10, 2000, orders constitute the trial court's rulings on appellants' requests for arbitration. Generally, "[a] trial court's oral ruling on a motion does not become effective until it is filed in writing

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[7] Medipace and Dr. Gura do not discuss or refer to this ruling, insofar it represents a denial of their objections to the February 10, 2000 order, and thus they have waived any contention of error regarding it. (*Tiernan v. Trustees of Cal. State University & Colleges* (1982) 33 Cal.3d 211, 216, fn. 4.)

with the clerk or entered in the minutes" (*In re Marriage of Drake* (1997) 53 Cal.App.4th 1139, 1170). Furthermore, when the trial court directs that a written order should be prepared, "entry then consists of filing the signed order with the clerk" (7 Witkin, Cal. Procedure (4th ed. 1997) Judgment, § 55, p. 584).

Moreover, the record establishes that these orders denied Medipace and Dr. Gura's request for arbitration on the basis of, inter alia, the need to avoid conflicting rulings. Given the trial court's remarks on this issue at the hearing on the motion for reconsideration, we see no need to remand this matter for any reconsideration of the issue in light of our conclusions that (1) CHC is not entitled to arbitration and (2) the unfair business practices claim is nonarbitrable, insofar as it seeks injunctive relief.

In sum, the trial court correctly denied Medipace and Dr. Gura's petition to compel arbitration.

DISPOSITION

The orders are affirmed. The writ of supersedeas will remain in effect until the issuance of our remittitur.

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

CURRY, J.

We concur:

VOGEL (C.S.), P.J.

EPSTEIN, J.

IN THE COURT OF APPEAL OF THE
STATE OF CALIFORNIA
SECOND APPELLATE DISTRICT

DIVISION 4

June 24, 2003

Muzeyyen Balaban-Zilke
v.
Cigna Health Care of California, Inc.

B140672
Los Angeles County No. BC209255

THE COURT:

Petition for rehearing is denied.

cc: All Counsel
File

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**SUPERIOR COURT OF THE
STATE OF CALIFORNIA FOR THE
COUNTY OF LOS ANGELES**

MUZEYYEN BALABAN-ZILKE, Ph.D., individually and as successor-in-interest to BRAD ZILKE, Plaintiffs, vs. CIGNA HEALTHCARE OF CALIFORNIA, INC.; CIGNA HEALTHCARE, INC.; CIGNA HEALTH-PLAN OF SOUTHERN CALIFORNIA; MEDIPACE MEDICAL	**CASE NO. BC 209255** **~~[PROPOSED]~~ ORDER DENYING MOTION OF DEFENDANT CIGNA HEALTHCARE OF CALIFORNIA, INC. TO COMPEL ARBITRATION AND PETITION FOR ORDER REQUIRING PLAINTIFF TO ARBITRATE THE CONTROVERSY**

GROUP, INC.; VICTOR GURA, M.D. and DOES 1 THROUGH 100, INCLUSIVE, Defendants.	)	DATE: January 25, 2000 TIME: 9:00 a.m. DEPT: 51 TRIAL DATE: Not Set **Hon. Irving Feffer**

THE COURT, having considered the moving, opposing and reply papers with respect to the MOTION OF DEFENDANT CIGNA HEALTHCARE OF CALIFORNIA, INC. ("CIGNA") TO COMPEL ARBITRATION AND PETITION FOR ORDER REQUIRING PLAINTIFF TO ARBITRATE THE CONTROVERSY, having considered only admissible evidence (*Biljac Associates v. First Interstate Bank*, 218 Cal.App.3d 1410 [1990]) and having heard and considered the arguments of all counsel, now HEREBY ORDERS, FINDS AND DECREES the following:

CIGNA's Motion to Compel Arbitration and Petition For Order Requiring Plaintiffs To Arbitrate The Controversy is denied in its entirety.

CIGNA has not met its burden of establishing that there exists a written agreement to arbitrate the controversy. (*C.C.P.* § 1281.2, *See American Builders Association v. Au-Yang*, 226 Cal.App.3d 170, 178-179 [1990], *Melchor Investment Co. v. Rolm Systems*, 3 Cal.App.4th 587, 592 [1992], *Rule of Court* 371) The only complete agreement provided by CIGNA in support of its Petition is from the year 1998. The 1998 agreement does not apply to this case. The facts giving rise to the Complaint took place in 1996 and 1997, and earlier. CIGNA has thus not provided any complete or executed agreements from the relevant time

period and, therefore, has not met its evidentiary burden. Based on CIGNA's contention that relevant arbitration agreements exist for earlier years, the Court denies this portion of the Motion and Petition without prejudice.

However, even if CIGNA had provided a relevant arbitration agreement, the Court finds good cause for denying arbitration based on waiver. Specifically, the California Supreme Court has ruled that a medical insurer such as CIGNA waives its right to compel arbitration by failing to inform its insured in a timely manner of his or her right to seek arbitration of coverage disputes relating to the provision of medical services. (*Davis v. Blue Cross*, 25 Cal.3d 418 [1979]) Here, the Court finds that CIGNA neither informed the Plaintiffs at the time of the coverage dispute of the availability of arbitration nor did CIGNA inform the Plaintiffs as to how to initiate arbitration proceedings. CIGNA did not give Plaintiffs timely and meaningful notice of any arbitration procedure nor did it call to Plaintiffs' attention the potential remedy of arbitration when it rejected Plaintiffs' claims. Rather, CIGNA first contended that arbitration was available only after this suit was filed. (see Balaban-Zilke Decl., ¶¶ 3-9). Under *Davis*, such conduct renders any arbitration clause unenforceable and constitutes a pre-litigation waiver of any right to compel arbitration CIGNA otherwise could have asserted.

The Court also denies the Petition on the separate and distinct ground that, assuming there was an agreement to arbitrate, CIGNA has failed to comply with its express contractual obligations concerning arbitration, has materially breached those contractual provisions, and therefore waived its right to compel arbitration of an agreement it has materially breached. Specifically, CIGNA voluntarily

agreed in the relevant contract documents on which it relies to comply fully with the Knox-Keene Health Plan Service Plan Act (*Health & Safety Code* § 1340 et seq) (the "Knox-Keene Act").[1] Accordingly, CIGNA has agreed to be contractually bound by all of the provisions of the Knox Keene Act insofar as the arbitrability of this matter is concerned. These provisions include *Health & Safety Code* § 1363.1 and *Health & Safety Code* § 1363(a)(10). The Court finds that CIGNA in this instance did not comply with either *Health & Safety Code* § 1363.1 or with *Health & Safety Code* § 1363(a)(10), nor did CIGNA comply with its contractual obligations to make the disclosures set forth in these statutes.

In addition, the Court denies arbitration on the grounds that many of Plaintiffs' claims are not arbitrable, as a matter of law, after the California Supreme Court's recent decision in *Broughton v. CIGNA Healthplans*, 21 Cal.4th 1066 [Dec. 2, 1999]. Arbitration is primarily intended to deal with private disputes. Plaintiffs have alleged widespread and continuing conduct by CIGNA and have asserted numerous public interest claims under both the Consumer Legal Remedies Act (*Civil Code* § 1750 et. seq.) and the Unfair Competition Law (*Bus. & Prof. Code* § 17200 et seq) which contain broad-based private general attorney requests for injunctive relief and other equitable remedies such as disgorgement. These public interest claims are not arbitrable as a matter of law.

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[1] CIGNA's Petition admits that CIGNA is licensed pursuant to and has been permanently licensed under the Knox-Keene Act at all times since March, 1979. (Petition, ¶ 2)

The Court further determines that under the circumstances of this case as described above, in Plaintiff's papers, and for the reasons argued by Plaintiffs at the hearing, that the Federal Arbitration Act does not require arbitration of any of the claims asserted by Plaintiffs. The Court further adopts each of the other arguments made by Plaintiffs as a basis for its ruling.

Dated: FEB 10, 2000 /s/ Irving S. Feffer
Judge of the Superior Court

Submitted By:
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By /s/ Anthony Kornarens
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SUPERIOR COURT OF THE STATE OF CALIFORNIA FOR THE COUNTY OF LOS ANGELES

MUZEYYEN BALABAN-ZILKE, Ph.D., individually and as successor-in-interest to BRAD ZILKE, Plaintiffs, vs. CIGNA HEALTHCARE OF CALIFORNIA, INC.; CIGNA HEALTHCARE, INC., CIGNA HEALTHPLAN OF SOUTHERN CALIFORNIA; MEDIPACE MEDICAL GROUP, INC.; VICTOR GURA, M.D. and	**CASE NO. BC 209255** **~~[PROPOSED]~~ ORDER DENYING MOTION OF DEFENDANT CIGNA HEALTHCARE OF CALIFORNIA, INC. TO RECONSIDER ORDER DENYING CIGNA'S MOTION TO COMPEL ARBITRATION AND PETITION FOR ORDER REQUIRING PLAINTIFF TO ARBITRATE THE CONTROVERSY AND DENYING JOINDER THEREIN**

DOES 1 THROUGH 100, INCLUSIVE, Defendants.	**DATE**: March 31, 2000 **TIME**: 9:00 a.m. **DEPT**: 51 **TRIAL DATE**: Not Set **Hon. Irving Feffer**

THE COURT, having considered the moving, opposing and reply papers with respect to the MOTION OF DEFENDANT CIGNA HEALTHCARE OF CALIFORNIA, INC. ("CIGNA") TO RECONSIDER ORDER DENYING CIGNA'S MOTION TO COMPEL ARBITRATION AND PETITION FOR ORDER REQUIRING PLAINTIFF TO ARBITRATE THE CONTROVERSY, having considered only admissible evidence (*Biljac Associates v. First Interstate Bank*, 218 Cal.App.3d 1410 [1990]) and having heard and considered the arguments of all counsel, now HEREBY ORDERS, FINDS AND DECREES the following:

CIGNA's Motion to Reconsider Order Denying CIGNA's Motion to Compel Arbitration and Petition For Order Requiring Plaintiffs To Arbitrate The Controversy is denied in its entirety.

CIGNA has brought its Motion under *C.C.P.* §1008. *C.C.P.* §1008 contains very specific requirements. Particularly, under this statute, CIGNA must provide a satisfactory explanation as to why, in the exercise of reasonable diligence, CIGNA could not have obtained and provided as part of its original Motion and Petition to Compel Arbitration the evidence upon which CIGNA bases its request for reconsideration.

Here, CIGNA has not provided a satisfactory explanation as to why CIGNA was not previously in possession of

the evidence upon which its request for reconsideration is based, nor has CIGNA provided a satisfactory explanation for its failure to produce this evidence at an earlier time. Accordingly, the Court finds that CIGNA has not met the requirements of *C.C.P.* §1008 and declines to reconsider its prior Order on that basis. (*Blue Mountain Dev. Co. v. Carville*, 132 Cal.App.3d 1005, 1013 [1982])

Additionally, and assuming, arguendo, that CIGNA had satisfied the requirements of *C.C.P.* §1008 and thats its Motion was therefore procedurally proper, the evidence CIGNA has proffered on this Motion would not effect this Court's prior ruling.

For example, while CIGNA contends it has provided new evidence regarding disclosure forms, brochures, and enrollment forms, CIGNA still has not shown that the Plaintiffs in this case ever saw these materials. For example, the enrollment forms are blank, and CIGNA fails to provide any enrollment forms actually signed by the Plaintiffs. There is no direct evidence that Plaintiffs ever saw these documents or agreed to their terms, nor has CIGNA otherwise controverted the declaration of Plaintiff Muzzeyen Balaban-Zilke submitted by Plaintiffs in opposition to CIGNA's original Petition to Compel Arbitration. ("Balaban-Zilke Dec")

Similarly, even had CIGNA provided evidence that Plaintiffs ever saw or agreed to CIGNA's [sic] these materials, none of the documents satisfy CIGNA's obligation under *Davis v. Blue Cross*, 25 Cal.3d 418 [1979] contemporaneously with a coverage dispute to inform Plaintiffs of the availability of arbitration to resolve Plaintiffs' coverage dispute with CIGNA, and to inform Plaintiffs how to initiate arbitration proceedings. (*See* Balaban-Zilke Dec.

¶¶3-9). CIGNA has provided no evidence which overcomes this Court's findings on the Original Petition that CIGNA neither informed the Plaintiffs at the time of the coverage dispute of the availability of arbitration nor did CIGNA inform the Plaintiffs as to how to initiate arbitration proceedings (see Order of February 17, 2000. 2:16-20).

Finally, even assuming that the requirements of *C.C.P.* §1008 were met, and even assuming that CIGNA had provided evidence that Plaintiffs ever saw or agreed to the evidence upon which CIGNA's request for reconsideration is based and even assuming that CIGNA had provided evidence of it having notified Plaintiffs of the availability of arbitration contemporaneous with Plaintiffs' coverage dispute, this Court would, in the exercise of its discretion, still not order the case to arbitration. The Court is aware that it has the power to sever some portion of the case and send it to arbitration while retaining and staying another portion of the case. But, however, the Court is also aware that such a posture could result in conflicting rulings. Under the totality of the circumstances of this case, and given that the Plaintiffs' private attorney general claims are inarbitrable under *Broughton v. CIGNA Healthplans*, 21 Cal.4th 1066 [1999] in any event, the Court would exercise its discretion to order joinder of any arbitrable portions of the case with the non-arbitrable portions and order the whole case to be heard before this Court. (*Prudential Prop. & Casualty Inc. Co. v. Sup. Ct.*, 36 Cal.App.4th 275 [1995]; *C.B. Starr Co. v. Boston R.E. Corp.*, 190 Cal.App.3d 1637 [1985]; *Contra Costa County v. Kaiser Foundation Health Plan, Inc.*, 47 Cal.App.4th 237, *C.C.P.* §1281.2)

The Court further adopts each of the other arguments made by Plaintiffs as a basis for its ruling.

The Court also denies the related joinder of Medipace Medical Group, Inc. and Victor Gura, M.D. for each of the reasons set forth above and, additionally, for the reasons stated in Plaintiffs' Opposition thereto.

The status conference set for April, 2000 is off calendar in view of the fact that Medipace and Gura have demurred to Plaintiffs' Second Amended Complaint.

Dated: 5/19, 2000 /s/ Irving S. Feffer
Judge of the Superior Court
IRVING S. FEFFER

Submitted By:
KORNARENS & HOWARD

By /s/ Edward F. Howard
Edward F. Howard
Attorneys For Plaintiffs

Court of Appeal, Second Appellate District,
Division Four – No. B140672
S117325

IN THE SUPREME COURT OF CALIFORNIA

En Banc

(Filed Aug. 13, 2003)

MUZEYYEN BALABAN-ZILKE,
Plaintiff and Respondent,

v.

CIGNA HEALTHCARE OF CALIFORNIA INC,
Defendant and Appellant.

Petition for review DENIED.

The request for an order directing publication of the opinion is denied.

/s/ GEORGE
Chief Justice

No. 03-709

Supreme Court, U.S.
FILED
DEC 11 2003
OFFICE OF THE CLERK

In The
Supreme Court of the United States

CIGNA HEALTHCARE OF CALIFORNIA, INC.,

Petitioner,

vs.

MUZEYYEN BALABAN-ZILKE, Ph.D.,
INDIVIDUALLY AND AS
SUCCESSOR-IN-INTEREST TO BRAD ZILKE,

Respondent.

On Petition For A Writ Of Certiorari
To The California Court Of Appeal,
For The Second Appellate District, Division Four

RESPONDENT'S BRIEF IN OPPOSITION

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COUNTERSTATEMENT OF QUESTIONS PRESENTED

1) Whether Section 2 of the Federal Arbitration Act [*9 U.S.C. §2*] allows a State to create a standard that can revoke any contractual provision "upon such grounds as exist at law or equity" in order to secure a constitutional Due Process right to be offered a choice, in contracts of adhesion, between retaining the inalienable and sovereign right of access to courts and juries, or to voluntarily elect to waive such right in favor of private binding arbitration, thereby preventing the involuntary imposition upon the weaker party of mandatory arbitration alone?

2) Whether a Federal statutory preference for arbitration may supercede one's choice to retain his/her superior and inalienable constitutional right to court and jury access?

3) Whether *California Health & Safety Code §1363.1*, a statute regulating the business of insurance pursuant to the McCarran-Ferguson Act, reverse preempts the Federal Arbitration Act?

TABLE OF CONTENTS

Page

COUNTERSTATEMENT OF QUESTIONS PRESENTED i

TABLE OF AUTHORITIES iv

STATEMENT OF THE CASE 1

ARGUMENT 2

I. THE FOURTEENTH AMENDMENT DUE PROCESS RIGHT, AND THE NINTH AND TENTH AMENDMENTS, GUARANTEE PARTIES TO CONTRACTS OF ADHESION THE RIGHT TO CHOOSE RETENTION OF COURT/JURY ACCESS OR TO WAIVE THIS RIGHT IN FAVOR OF BINDING ARBITRATION 2

A. The Constitutional Right to Choose..... 4

B. Cigna Exercised its Procedural Right to Reject Jury Trial but Denied, with Approval by a Governmental Employer, Respondent's Substantive Due Process Right to Choose 8

C. Choice Is a Retained Right of Sovereignty 9

D. "Mandatory" is "Dictatory" 12

E. California Forbids the Assignment or Other Alienation of Intangible Interests 14

F. Mandatory Arbitration is not an Alternative Neutral Forum Because it Lacks any Residuum of Sovereignty..... 16

TABLE OF CONTENTS – Continued

Page

II. CALIFORNIA HEALTH & SAFETY CODE §1363.1 IS A STATUTE THAT REGULATES THE BUSINESS OF INSURANCE PURSUANT TO THE MCCARRAN-FERGUSON ACT AND THEREFORE REVERSE PREEMPTS THE FEDERAL ARBITRATION ACT 20

A. The FAA is a law of General Applicability 23

B. California's Mandatory Disclosure of Waiver of the Constitutional Right to Court and Jury Access Is a State Law Regulating the Business of Insurance Within the Meaning of the McCarran-Ferguson Act 23

1. California Health and Safety Code §1363.1 Transfers or Spreads Policyholder Risk Between the Policyholder and the Insurer 24

2. California Health & Safety Code §1363.1 Affects an Integral Part of the Policy Relationship Between the Insurer and the Insured by Protecting the Policyholders' Interest & Controlling the Terms of the Contract 26

3. The Provisions of California Health & Safety Code §1363.1 Are Exclusively Limited to Entities Within the Insurance Industry 28

CONCLUSION 28

TABLE OF AUTHORITIES

Page

CASES

Armendariz v. Foundation Health, 99 Cal.Rptr.2d 745, 24 Cal.4th 83 (2000) 19

Boozell v. United States, 979 F. Supp. 670 (N.D. Ill. 1997) 26

Broughton v. CIGNA Healthplans, 21 Cal.4th 1066, 90 Cal.Rptr.2d 334 (1999) 11

Circuit City Stores, Inc. v. Mantor, 335 F.3d 1101 (2003) 11

Cohens v. Virginia, 19 U.S. 264 (1821) 4

County of Riverside v. Superior Court, 132 Cal.Rptr.2d. 713, 30 Cal.4th 278 (2003) 13

Davister Corp. v. United Republic Life Insurance Company, 152 F.3d 1277 (10th Cir. 1998) 23

D.H. Overmyer Co., Inc. v. Frick Co., 405 U.S. 174 (1972) 3, 12

Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205 (1979) 27

Humana Inc. v. Forsyth, 525 U.S. 299 (1999) 22

In re Pfahler, 88 P. 270, 150 Cal. 71 (1906) 29

Johnston v. Paul Revere Life Ins. Co., 241 F. 3d 631 (8th Cir. 2001) 28

Kentucky Ass'n of Health Plans v. Miller, 123 S.Ct. 1471 (2003) 24

Lawrence v. Texas, ___ U.S. ____, 123 S.Ct. 2472 (2003) 4

Mathis v. Auto Club Inter-Insurance Exchange, 410 F. Supp 1037 (W.D. Mo. 1976) 26

TABLE OF AUTHORITIES – Continued

Page

McMillan v. Sup. Ct., 57 Cal.Rptr.2d 674 (1996).....19

Moncharsh v. Heily & Blase, 10 Cal.Rptr.2d 183, 3 Cal.4th 1 (1992).....14

Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983).....20

Munich American Reins. Co. v. Crawford, 141 F.3d 585 (5th Cir. 1998), *cert. denied*, 119 S.Ct. 539 (1998).....21, 22

Murphy v. Allstate Ins. Co., 132 Cal.Rptr. 424, 17 Cal.3d 937 (1976).....14

Mutual Reinsurance Bureau v. Great Plains Mut. Ins. Co., 969 F.2d 931 (10th Cir. 1992).....24

Nat'l Paint & Coatings Ass'n v. City of Chicago, 45 F.3d 1124 (7th Cir.1995).....4

Pardee Const. Co. v. Superior Court, 123 Cal.Rptr.2d 288, 100 Cal.App.4th 1081 (2002).....13

People v. Collins, 26 Cal.4th 297, 109 Cal.Rptr.2d 836 (2001).....12

People v. One 1941 Chevrolet Coupe, 231 P.2d 832, 37 Cal.2d 283 (1951).....12

Prudential Ins. Co. v. Benjamin, 66 S.Ct. 1142 (1946).....21

SEC v. Variable Annuity Life Ins. Co. of America, 359 U.S. 65 (1959).....21

R.J. Reynolds Tobacco Co., et al. v. Bonta, et al., 272 F.Supp.2d 1085 (2003).....4

Rush Prudential HMO, Inc. v. Moran, 536 U.S. 355 (2002).....28

TABLE OF AUTHORITIES – Continued

Page

SEC v. National Securities, Inc., 393 U.S. 453 (1969) 26

Smith v. PacifiCare Behavioral Health of California, Inc., 93 Cal.App.4th 139, 113 Cal.Rptr.2d 140 (2001), *cert. denied*, 537 U.S. 818 (2002) 20, 29

Steffens v. National Distillers and Chemical Corp., 69 F.3d 1226 (2nd Cir. 1995) 21

Stephens v. American Intl. Ins. Co., 66 F.3d 41 (2nd Cir. 1995) 23

Union Oil Co. of California v. Hane, 80 P.2d 516, 27 Cal.App.2d 106 (1938) 30

Unum Life Ins. Co. of America v. Ward, 526 U.S. 358 (1999) 23, 27

U.S. v. Sylvanus, 192 F.2d 96 (7th Cir. 1951) 21

U.S. Dept. of Treasury v. Fabe, 508 U.S. 491 (1993) 21, 26, 27

Zelson v. Phoenix Mut. Life Ins. Co., 549 F.2d 62 (8th Cir. 1977) 26

CONSTITUTIONS

United States Constitution amend. IX 10

United States Constitution amend. X 9, 10

United States Constitution amend. XIII 4

United States Constitution amend. XIV 2

United States Constitution amend. XIV, §4 5

California Constitution, art. 1, §1 12

California Constitution, art. 1, §7(b) 15

TABLE OF AUTHORITIES – Continued

Page

California Constitution, art. 1, §16 12
California Constitution, art. 1, §24 11
California Constitution, art. 2, §1 15
California Constitution, art. 11, §11 13

STATUTES

9 U.S.C. §2 ..... 10, 21, 30
15 U.S.C. §12(b) 21
Cal. Civ. Code §43 15
Cal. Civ. Code §1565 11
Cal. Civ. Code §1708 15
Cal. Civ. Code §3275 10
Cal. Civ. Code §3510 15
Cal. Civ. Code §3513 15
Cal. Civ. Code §3514 15
Cal. Civ. Code §3517 15
Cal. Civ. Code §3520 15
Cal. Civ. Code §3528 15
Cal. Gov. Code §100 15
California Health & Safety Code §1363.1 ..... *passim*
California Health & Safety Code §1389.2 10
California Health & Safety Code §123205 10

TABLE OF AUTHORITIES – Continued

Page

MISCELLANEOUS

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TABLE OF AUTHORITIES – Continued

Page

The Records of the Federal Convention of 1787 (Max Farrand ed., 1937)..... 6

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Karl A. Slaikeu and Diane W. Slaikeu, Confidential from General Counsel to Ceo: "I'm Fed Up, and We're Not Going to Take This Anymore!", 5 J. Health Care L. & Pol'y 335 (2002).....25

STATEMENT OF THE CASE

Muzeyyen Balaban-Zilke, Ph.D. was a Los Angeles County employee at all times relevant herein. As a benefit of her employment with the County of Los Angeles, she was annually offered six health care plans by her employer. With the approval of her governmental employer, none of these health care plans offered her a choice between retaining the State civil jury right or waiving it in favor of binding arbitration. Rather, all health care plans offered to each and every County employee, including the CIGNA plan chosen by Balaban-Zilke, required the signing of a mandatory arbitration clause. Despite Balaban-Zilke's entitlement to health care coverage as a benefit of employment, no such coverage could be offered to any County employee unless all 80,000 County employees agreed to mandatory arbitration. No County employee was allowed to reserve, nor was any County employee, including Balaban-Zilke, informed of his/her right to reserve, without forfeiture of entitled benefits, the civil jury guarantee when enrolling in any County-offered health care plan. Part of the State Court record is a declaration under penalty of perjury by a Los Angeles County supervisor which states that despite an entitlement to health care coverage, no such coverage could be offered to any County employee unless each employee agreed to *mandatory* arbitration. (Declaration of Nidu Permaul, Respondent's App. 1); (Domestic Partner Enrollment and Change Form, Respondent's App. 5); (Declaration of Muzeyyen Balaban-Zilke, Respondent's App. 8). Petitioner CIGNA concedes that Respondent "could not have obtained coverage" without signing a mandatory arbitration clause. (Pet. brief at page App. 16).

ARGUMENT

I. THE FOURTEENTH AMENDMENT DUE PROCESS RIGHT, AND THE NINTH AND TENTH AMENDMENTS, GUARANTEE PARTIES TO CONTRACTS OF ADHESION THE RIGHT TO CHOOSE RETENTION OF COURT/JURY ACCESS OR TO WAIVE THIS RIGHT IN FAVOR OF BINDING ARBITRATION

California *Health & Safety Code §1363.1* mandates that health care plans "shall include" a minimum standard of disclosure concerning the waiver of one's constitutional right to jury. This minimum disclosure empowers the prospective enrollee to exercise a constitutional right to choose a competing health care plan that does not mandatorily impose arbitration as the lone form of administering justice. This constitutional right to choose was totally denied to Muzeyyen Balaban-Zilke because all health care plans offered to her by her governmental employer contained mandatory arbitration clauses. Petitioner CIGNA concedes that Respondent "could not have obtained coverage" without signing a mandatory arbitration clause. (Pet. brief at page App. 16). *See also*, (Declaration of Nidu Permaul, Respondent's App. 1); (Domestic Partner Enrollment and Change Form, Respondent's App. 5); (Declaration of Muzeyyen Balaban-Zilke, Respondent's App. 8).

Respondent contends that she had an individual reserved right to exercise her conscience, without inapposite compulsion or restriction, to choose to retain her right to court and jury access in the event of a yet unknown future dispute with CIGNA. It is also her contention that no other natural or artificial citizen can condition an unguaranteed economic benefit on the involuntary surrender, without choice, of a superior and inalienable individual political liberty. The exercise of this right of conscience is freely "beyond the legitimate reach of sovereignty" or government. James Madison on Sovereignty (1835), 9 *The*

Writings of James Madison, at 570-1 (Gaillard Hunt ed.) (1910).

"The Supreme Court has considered only one instance of a contractual waiver of due process rights in a commercial setting." 3 Ronald D. Rotunda & John E. Nowak, Treatise on Constitutional Law: Substance and Procedure 162 (3rd ed. 1999).

In *D.H. Overmyer Co., Inc. v. Frick Co.*, 405 U.S. 174 (1972):

> [T]he Court upheld a waiver of process clause which had been negotiated in a contract between two independent businesses. However, the Court did not indicate that it would be willing to uphold such waivers of process when it was unclear if the parties had truly bargained over the provision. Thus the validity of form contract provisions by which one party waives his rights to notice or process remains an open question. If the Court were to apply the 'knowing and intelligent' waiver standard of the criminal cases it would be virtually impossible to uphold such provisions where the parties were of clearly unequal bargaining strength or where there was no real attempt to inform the debtor [or other weaker party] of the meaning of the provision.

3 Ronald D. Rotunda & John E. Nowak, Treatise on Constitutional Law; Substance and Procedure 162 (3rd ed. 1999).

As noted by this Court in *Overmyer*, "where the contract is one of adhesion, where there is great disparity in bargaining power . . . other legal consequences may ensue" to make unenforceable forced waivers of due process rights. 405 U.S. at 188.

An individual's Fourteenth Amendment due process right in favor of liberty of choice does not extend to corporations like CIGNA, and hence is superior to any lesser right upon which CIGNA claims preemption. As one

district court recently noted when distinguishing between an individual's liberty interest and a corporation's procedural due process right: "'[c]orporations do not have fundamental rights; they do not have liberty interests, period.' *Nat'l Paint & Coatings Ass'n v. City of Chicago,* 45 F.3d 1124, 1129 (7th Cir.1995). Corporations do have property interests, however, that may be protected by procedural due process." *R.J. Reynolds Tobacco Co., et al. v. Bonta, et al.*, 272 F.Supp.2d 1085, 1111 (2003).

A. THE CONSTITUTIONAL RIGHT TO CHOOSE

Recently, this Court found that one's due process liberty right extended to a right of choice in the area of private sexual relationships beyond the ability of government to regulate. *Lawrence v. Texas*, ___ U.S. ___, 123 S.Ct. 2472, 2478, 2481, 2483 (2003).

Under our Constitution "[t]he people . . . cede . . . [only] some of their natural rights" to government. The Federalist No. 2, at 37 (John Jay) (Clinton Rossiter ed., 1961). This Court has found that "the opinion of the Federalist has always been considered as of great authority" *Cohens v. Virginia*, 19 U.S. 264, 418 (1821). In addition, "government is instituted no less for protection of the property than of the persons of individuals." The Federalist No. 54, at 339 (James Madison) (Clinton Rossiter ed., 1961)

Natural rights of freedom and liberty have traditionally been based upon the notion of a birthright which is not absolutely surrendered to government and which takes priority over property rights in the event of a direct and unavoidable conflict. For instance, a former slaveholder's loss of property and increased financial obligation to economically compensate former slaves following the ratification of the Thirteenth Amendment could not support a claim for breach of contract or indemnity: "any

claim for the loss of emancipation of any slave . . . shall be held illegal and void." *U.S. Const. Amend. XIV, §4.*

Similarly, the common law during the Founding Era distinguished between commercial rights and obligations, on the one side, and natural rights, on the other side, based upon a notion that the former was related to the consent of a limited number, such as merchants, while the latter was related to the consent of the people at large. More specifically, the common law in 1791 expressly stated that economic "special customs," such as "the custom of merchants," must fall or be narrowly construed when "in derogation of the common law," because the common law reflected the consent of all of society, while "special customs" only reflected the consent of a limited economic class, i.e., merchants. 1 William Blackstone, *Commentaries on the Law of England* 78 (London, 1st ed., 1765); reprinted (Stanley N. Katz introduction, University of Chicago Press, 1979); *see also, id.* at 73.

This concept of liberty interests preempting property interests in the event of a direct and unavoidable conflict can also be found in James Madison's view that the states, rather than the federal government, would remain the primary venue for protecting individual liberties. For instance, the federal government "will be exercised principally on external objects, as war, peace, negotiation and foreign commerce" while the "numerous and indefinite" powers reserved to the several states "will extend to all the objects, which, in the ordinary course of affairs, concern the lives, liberties, and properties of the people; and the internal order, improvement, and prosperity of the State." The Federalist No. 45, at 292-3 (James Madison) (Clinton Rossiter ed., 1961).

According to James Madison, the "meaning of the power to regulate commerce is to be sought in the general use of the phrase." In this regard, there was an "external

object" as to why the states did not intend to "annihilate" the federal interstate commerce power, and this external object was to not "disarm the nation from protecting occupations and establishments, important to its defense and independence, against the subversive policy of foreign Rivals or Enemies." Letter from James Madison to Joseph C. Cabell (Mar. 22, 1827), 9 *The Writings of James Madison*, at 284-5 (Gaillard Hunt ed.) (1910).

Madison later wrote that the purpose of the U.S. Constitution was to give "all the attributes of a national government in its relations with other Nations, including the most essential one, of regulating foreign Commerce . . . " Letter from James Madison to John Tyler (1833), 9 *The Writings of James Madison*, at 509 (Gaillard Hunt ed.) (1910).

During the ratification debates over the U.S. Constitution, Madison wrote that without the interstate commerce clause, "the great and essential power of regulating foreign commerce would have been incomplete and ineffectual." The Federalist No. 42, at 267 (James Madison) (Clinton Rossiter ed., 1961). As to the protection of civil liberties, the states would retain "a residuary and inviolable sovereignty." The Federalist No. 39, at 245 (James Madison) (Clinton Rossiter ed., 1961).

When drafting the Constitution, Roger Sherman, the only Founder to sign all four major founding instruments, acknowledged the purpose behind the interstate commerce clause when declaring that "the oppression of the uncommercial states was guarded against by the power to regulate trade between the States." 2 *The Records of the Federal Convention of 1787*, at 308 (Max Farrand ed., 1937) (reprinted Yale University Press, 1966).

The intent of the interstate commerce clause, the basis for the Federal Arbitration Act, was to prevent economic jealousies between states when acting in their

corporate capacities; a capacity unrelated to the protection of the reserved liberty relationship between the individual and any government.

In other words, the Founders did not intend to empower the federal government to use economic laws arising out of the commerce power, the primary end of which was to advance foreign policy and prevent related interstate jealousies, as a means to "annihilate" otherwise preexisting and "domestic" individual political liberties. It was this political view that caused Madison to note that while the majority, when exercising powers of sovereignty, "may do anything that could be *rightfully* done by the unanimous concurrence of the members; *the reserved rights of individuals* (of conscience for example) in becoming parties to the original compact *being beyond the legitimate reach of sovereignty*, wherever vested or however viewed." (emphasis added) James Madison on Sovereignty (1835), 9 *The Writings of James Madison*, at 570-1 (Gaillard Hunt ed.) (1910). For this reason, CIGNA cannot argue, even implicitly, that the FAA majority faction can sacrifice "the public good and the rights of other citizens." The Federalist No. 10, at 80 (James Madison) (Clinton Rossiter ed., 1961).

Consistent with one's reserved right to freely exercise his conscience, including the subject right to choose, is our republican premise that justice, not property, "is the end of government . . . the end of civil society." Justice must be deemed the proper end of government, otherwise "the stronger faction can readily unite and oppress the weaker." The Federalist No. 51, at 324 (James Madison) (Clinton Rossiter ed., 1961).

B. CIGNA EXERCISED ITS PROCEDURAL RIGHT TO REJECT JURY TRIAL BUT DENIED, WITH APPROVAL BY A GOVERNMENTAL EMPLOYER, RESPONDENT'S SUBSTANTIVE DUE PROCESS RIGHT TO CHOOSE

In the instant matter, although its corporate status disqualified it from possessing fundamental liberty interests, CIGNA nevertheless made its own unilateral choice to either retain the civil jury or surrender it in favor of a mandatory arbitration clause. CIGNA chose to surrender the civil jury. However, CIGNA and all other health care plans did not reciprocate with regard to all Los Angeles County employees, including Respondent. No choice was offered by these health care plans to these 80,000 employees, who did possess fundamental liberty interests, including the right to choose court and jury access in the event of injuries caused by the unreasonable denial of medically necessary care. (Declaration of Nidu Permaul, Respondent's App. 1); (Domestic Partner Enrollment and Change Form, Respondent's App. 5); (Declaration of Muzeyyen Balaban-Zilke, Respondent's App. 8). Petitioner CIGNA concedes that Respondent "could not have obtained coverage" without signing a mandatory arbitration clause. (Pet. brief at page App. 16).

No artificial corporation in the business of marketing contracts of adhesion in health care should be allowed the power to condition this mere contractual benefit on the coerced surrender by the individual enrollee of an inalienable political right to choose court and jury access. To do so is worse than illegal consideration, it is unconstitutional consideration. As noted by James Madison, "power wherever lodged, is liable more or less to abuse." Letter from James Madison to Thomas Lehre (Aug. 2, 1828), 9 *The Writings of James Madison*, at 315 (Gaillard Hunt ed.)

(1910). This absence of choice unconstitutionally denies a right to mutuality of consent.

C. CHOICE IS A RETAINED RIGHT OF SOVEREIGNTY

The Ninth Amendment to the United States Constitution acknowledges that unenumerated rights are "retained by the people." The Tenth Amendment to the United States Constitution acknowledges that undelegated powers "are reserved to the states respectively or to the people." By this is meant that "the real parties to the constitutional compact of the United States are the *States* – that is, the people thereof respectively in their sovereign character, and they *alone* . . ." (emphasis in the original). Outline of James Madison (Sept. 1829), 9 *The Writings of James Madison*, at 352 (Gaillard Hunt ed.) (1910). *See also, id.* at 356. Stated differently, "the Constitution was created by the people, but by the people as composing distinct States, and acting by a majority in each." The "sovereign or supreme powers of the Government are divided into the separate depositories of the Government of the U.S. and the Government of the individual States." Letter from James Madison to M.L. Hurlbert (May 1830), 9 *The Writings of James Madison*, at 373 (Gaillard Hunt ed.) (1910). Not even the treaty power enables the federal government to change the domestic republican character of our state and federal governments, because the people did not delegate, but rather retained, such unlimited powers.

As observed by the editor of The Documentary History of the Ratification of the Constitution, the purpose behind amending the Constitution, including its interstate commerce clause, was to "clarify the federal-state relationship and guarantee the rights of individuals." John P. Kaminski, *Restoring the Grand Security: The Debate Over*

a Federal Bill of Rights, 1787-1792, 33 Santa Clara L.Rev. 887, 903 (1993) (citing to Bernard Schwartz, 2 *The Bill of Rights: A Documentary History*, 762 (1971)).

In short, the FAA recognizes the powers delegated to the States by the Ninth and Tenth Amendments to the U.S. Constitution. Thus, the FAA confirms the States' constitutional power to revoke commercial provisions "upon such grounds that exist at law or equity" [*9 U.S.C. §2*] *not* because of a will to discriminate against arbitration per se, but because of a will to deter the involuntary, unknowing or "mandatory" surrender, without choice, of any superior and state guaranteed individual political liberty.

Protecting an individual's right of choice in order to avoid an involuntary, coerced and unknowing forfeiture of that right in contracts of adhesions does not impact (because it is conceptually unrelated to) interstate commerce, particularly considering the state's exclusive jurisdiction in determining whether subscriber fees charged for an enrollee's reservation of the civil jury right are, for example, actuarially sound. *California Health & Safety Code §§1389.2, 123205*. Moreover, "equity abhors a forfeiture." 11 B.E. Witkin, *Summary of California Law* (9th ed.), Equity §18 at 695 (1990); *see also, Cal. Civ. Code §3275*.

Relying, in part, on California authority, the Ninth Circuit recently invalidated an arbitration clause on the grounds that it was oppressive and unconscionable given the fact that it was imposed, without choice of retaining court and jury access, under the threat of dismissal from employment:

> a meaningful opportunity to negotiate or reject the terms of a contract must mean something more than an empty choice. At a minimum, a party . . . must have an actual, meaningful, and reasonable choice to exercise that discretion. In

> light of Circuit City's insistence that Mantor sign the arbitration agreement – under pain of forfeiting his future with the company – the fact that in 1995 Mantor was presented with an opt-out form does not save the agreement from being oppressive, for Mantor had no meaningful choice, nor any legitimate opportunity, to negotiate or reject the terms of the arbitration agreement . . . Accordingly, because Circuit City presented the arbitration agreement to Mantor on an 'adhere-or-reject' basis we conclude that the arbitration agreement was procedurally unconscionable.

Circuit City Stores, Inc. v. Mantor, 335 F.3d 1101, 1106-7 (2003).

California courts have acknowledged that "the purpose of arbitration is to *voluntarily* resolve private disputes . . ." [emphasis added] *Broughton v. CIGNA Healthplans*, 21 Cal.4th 1066, 1080, 90 Cal.Rptr.2d 334, 344 (1999). In order for consent to a contract to be valid, it must be "free, mutual and communicated by each to the other." *Cal. Civ. Code §1565*. Respondent contends that her due process right empowers state courts to find ways to invalidate contracts that deny one the choice to freely retain inalienable liberties, rather than being compelled to waive them in favor of an unguaranteed and inferior replacement, whatever the nature may be of that replacement.

California's Constitution expressly declares that the rights guaranteed by it "are not dependent on those guaranteed by the United States Constitution." *Cal. Const. art. 1, §24*. It also states that its "declaration of rights may not be construed to impair or deny others retained by the people." *Id.*

Unlike the federal constitution, the California Constitution embraces the word "inalienable" when expressly declaring under its Declaration of Rights that "all people

are by nature free and independent and have inalienable rights. Among these are enjoying and defending life and liberty, acquiring, possessing and protecting property, and pursuing and obtaining safety, happiness, and privacy." *Cal. Const. art. 1, §1.* Under its Declaration of Rights, the California Constitution also guarantees one's right to a civil jury as being "inviolate," and without any qualifying reference to the common law. *Cal. Const. art. 1, §16.*

D. "MANDATORY" IS "DICTATORY"

Under California law, the state may not punish a criminal defendant for the exercise of a constitutional right to a jury, or promise leniency to a defendant for refraining from the exercise of that right, whether the source of such coercion is executive, legislative, or judicial in nature. *People v. Collins*, 26 Cal.4th 297, 299, 109 Cal.Rptr.2d 836, 842 (2001). The basis of this decision was to assure that any waiver of a constitutional right must be done freely, voluntarily, knowingly, and without compulsion. *Accord, D.H. Overmyer Co., Inc v. Frick Co.,* 405 U.S. 174 (1972). Contrary to this rationale is the notion of *mandatory* arbitration in the civil sector.

"Mandatory" means "required or commanded by authority; obligatory," The American Heritage College Dictionary 823 (3d ed. 1993), or "of, relating to, or constituting a command; required; preemptory." Black's Law Dictionary 973 (7th ed. 1999). In other words, "mandatory" connotes that one does not have a choice to retain even a preexisting "inalienable" and "inviolate" political right. For this reason, *mandatory* arbitration violates Respondent's constitutional due process right to be offered a choice between jury or arbitration before freely choosing one over the other, especially when enforced by government. Any legislative attempt to abridge the constitutional right to trial by jury is void. *See, People v. One 1941 Chevrolet*

Coupe, 231 P.2d 832, 835, 37 Cal.2d 283, 287 (1951). The "discrimination" at issue is not against arbitration per se, but rather against the mandatory, unknowing and involuntary nature of its imposition.

In protecting an individual's inviolate state constitutional right to a civil jury in real estate contracts of adhesion, California courts have invalidated as unconscionable "judicial reference" alternatives to the civil jury whenever home-buyers are offered this inferior and unguaranteed alternative in the presence of "little choice," i.e., through a "take-it-or-leave-it proposition." *Pardee Const. Co. v. Superior Court*, 123 Cal.Rptr.2d 288, 292-3, 100 Cal.App.4th 1081, 1087 (2002).

Recently, the California Supreme Court struck down a binding arbitration clause on the premise that a governmental entity was denied choice, framing the issue as follows: "the issue is not whether a county may *voluntarily* submit compensation issues to arbitration, . . . but whether the Legislature may *compel* a county to submit to arbitration *involuntarily*." [emphasis added] *County of Riverside v. Superior Court,* 132 Cal.Rptr.2d 713, 718, 30 Cal.4th 278, 284 (2003). In addition, the California Supreme Court also relied upon *Art. 11, §11*, of the California Constitution which states that "[t]he Legislature may not delegate to a private person or body power . . . to levy taxes . . . or perform municipal functions." *County of Riverside,* 132 Cal.Rptr.2d at 724, 30 Cal.4th at 291.

Respondent contends that delegating the administration of justice to a mandatory arbitrator without first offering to the enrollee a choice to retain the civil jury right, is violative of the Respondent's due process right to choose jury waiver voluntarily, freely, knowingly and without compulsion. Furthermore, the administration of justice via the resolution of private disputes is a traditionally public "municipal function."

Mandatory arbitration without choice unconstitutionally forces enrollees to be double taxed: first with a tax for a court system that has been denied them; second with a "tax" in the form of an arbitrator fee to replace an otherwise free Superior Court judge. Lastly, to enforce *mandatory* arbitration, when compelled without choice, would adopt the anti-republican model of tyranny given the concentration of all three branches of government into the hands of one mandatory arbitrator, whose errors in fact or law are not reviewable in the California Superior Courts. *See, Moncharsh v. Heily & Blase*, 10 Cal.Rptr.2d 183, 184, 188, 200, 3 Cal.4th 1, 6, 11, 28 (1992). "The accumulation of all powers legislative, executive, and judiciary, in the same hands . . . may justly be pronounced the very definition of tyranny." The Federalist No. 47, at 301 (James Madison) (Clinton Rossiter ed., 1961).

E. CALIFORNIA FORBIDS THE ASSIGNMENT OR OTHER ALIENATION OF INTANGIBLE INTERESTS

In California, contract claims are assignable, but personal tort claims are not. *Murphy v. Allstate Ins. Co.*, 132 Cal.Rptr. 424, 427, 17 Cal.3d 937, 942 (1976). In relation, *mandatory* arbitration in this contract of adhesion unconstitutionally violated Respondent's similarly intangible due process right to choice by forcing an assignment of the administration of justice away from civil courts and juries and toward a mandatory arbitrator, without any constitutionally equal consideration being received by the enrollee. It is the position of the Respondent that the right to choose between civil jury and non-mandatory arbitrator is a right of conscience that is constitutionally immune from forced alienation. To believe otherwise is to believe that our guaranteed individual liberties are no longer priceless, inalienable and inviolate.

California recognizes certain basic and general notions of due process fairness that place the preservation of fundamental political rights above all else when those rights are threatened. While arbitration in and of itself does not threaten California liberties, *mandatory* arbitration does by denying choice.

If this Court accepts the premise that the powerful party in a contract of adhesion cannot compel (by denying choice) the weaker party to surrender a constitutional right to jury, then the meanings of certain maxims of California jurisprudence are not denigrated. For instance, "one must so use his own rights as not to infringe upon the rights of another." *Cal. Civ. Code §3514.* "No one should suffer by the act of another." *Cal. Civ. Code §3520.* "No one can take advantage of his own wrong." *Cal. Civ. Code §3517.* "[A] law established for a public reason cannot be contravened by a private agreement." *Cal. Civ. Code §3513.* "Every person is bound, without contract, to abstain from injuring the person or property of another, or infringing upon any of his rights." *Cal. Civ. Code §1708.* "[E]very person has . . . the right of protection . . . from personal insult . . ." *Cal. Civ. Code §43.* "The law respects form less than substance." *Cal. Civ. Code §3528.* "All political power is inherent in the people. Government is instituted for their protection, security, and benefit . . ." *Cal. Const. art. 2, §1.* "A citizen or class of citizens may not be granted privileges or immunities not granted on the terms to all citizens." *Cal. Const. art. 1, §7(b).* "The sovereignty of the state resides in the people thereof . . ." *Cal. Gov. Code §100.* "When the reason of a rule ceases, so should the rule itself." *Cal. Civ. Code §3510.*

F. MANDATORY ARBITRATION IS NOT AN ALTERNATIVE NEUTRAL FORUM BECAUSE IT LACKS ANY RESIDUUM OF SOVEREIGNTY

Given the denial of choice, mandatory arbitration does not constitute an alternative neutral forum because a mandatory arbitrator does not reflect divided and checked power, a hallmark of republican government, nor does he possess any constitutional and residuary element of sovereignty. Hence, the enrollee does not receive any constitutionally equivalent consideration at the moment of forfeiting constitutional rights for a mere economic benefit.

James Wilson noted that the civil jury right had "a superiority over any other mode" in the administration of justice. He knew "no mode of investigation equal to that by a jury: they hear everything that is alleged; they not only hear the words but they see and mark the features of the countenance; they can judge of weight due to such testimony; and moreover, it is a cheap and expeditious manner of distributing justice. There is another advantage annexed to the trial by jury; the jurors may indeed return a mistaken or ill-founded verdict, but their errors cannot be systematical." 2 *The Debates in the Several State Conventions on the Adoption of the Federal Constitution*, Penn. Ratification Debates 516 (Jonathan Elliot ed., Reprint ed., Ayer Co. 1987).

Wilson also wrote that every citizen, when acting as a juror, "forms a part of the sovereign power." 1 *The Works of James Wilson* 73 (Robert Green McCloskey ed., 1967). This is so because "the supreme or sovereign power of the society resides in the citizens at large." *Id.* at 77. In the administration of justice, sovereignty is "partly delegated [to judges] and partly retained" by the sovereign people as jurors. *Id.* at 174, 2 *The Works of James Wilson* 547 (Robert Green McCloskey ed., 1967). Jurors realize the

maxim that "a free people are governed by laws, of which they approve." 1 *The Works of James Wilson* 179 (Robert Green McCloskey ed., 1967). Precedent to approval is choice. Because jurors possess that residuum of sovereignty that is "supreme, arbitrary, absolute, uncontrollable," 2 *The Works of James Wilson* 506 (Robert Green McCloskey ed., 1967), they serve as a "check" against the "esprit du corps" of judges. *Id.* at 541-2.

To avoid the "esprit du corps" of arbitrators, Wilson explained that only *post-dispute* "arbitrations might be as valid as the judgments of courts," so long as the parties "sign a reference of the matter in controversy to the peace makers so chosen," and the reference is "ratified by the county court." *Id.* at 471.

Wilson's federalist view of sovereignty was reflected in the drafting history of the Tenth Amendment relative to the addition of the phrase "or to the people." This phrase was added and approved over an objection that it "tended to create a distinction [which it did] between the people and their legislatures." *Creating the Bill of Rights: The Documentary Record from the First Federal Congress* 193, 199 (Helen E. Veit et al. eds. 1991).

When proposing the civil jury and other "great rights of mankind" before the First Federal Congress, Madison acknowledged that the primary cause of disaffection with the Constitution was that it did not contain any "effectual provision against encroachments on particular rights, and those safeguards which they have been long accustomed to have *interposed between them [as sovereign] and the magistrate who exercised [by delegation] the sovereign power*." (emphasis added) *Id.* at 79.

Similarly, Richard Henry Lee, the former President of Congress, observed that the administration of justice without guaranteed civil jurors was the first "step towards establishing aristocracy [as the sovereign]; the most

oppressive of all governments." Richard Henry Lee, Esq., *Virginia Gazette*, Dec. 22, 1787; [reprinted in 5 *The Complete Anti-Federalist* 114 (Herbert J. Storing ed., 1981)], (borrowing from 3 William Blackstone, *Commentaries on the Law of England* 379-80 (London, 1st ed., 1765)); reprinted (Stanley N. Katz introduction, University of Chicago Press, 1979).

United States Senator Russell D. Feingold, Chair of the Subcommittee on the Constitution of the Senate Committee on the Judiciary, has also recently pronounced the profound constitutional distinction "between arbitration that is 'mandatory' and 'voluntary.'" Senator Russell D. Feingold, *Mandatory Arbitration: What Process Is Due?*, 39 Harv. J. on Legis. 281, 283 (2002).

It is common knowledge that private retired judges, charging $5,000 to $7,500 per day, receive all of their repeat business not from consumers, but from businesses. This self-interest is inconsistent with the people's declared expectation of impartiality.

As one unanimous California Court of Appeal observed in an opinion ordered depublished:

> [T]he public purse-strings remain tightly knotted while litigants are given the privilege of paying twice – first through taxation, then again through a user's fee disguised as payment for a referee [or other private judge] . . . [O]ur courts are experiencing the wholesale departure of judges from the public system to the greener pastures of private judging, where they can and do earn more money, receive more help, obtain better accommodations, and work as many or as few hours as they choose.
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> * * *
>
> [W]e are too fast approaching the time when the law, in its majestic equality, will forbid the poor from using not only a private system restricted to

> the wealthy, but also the public system theoretically available to all.

McMillan v. Sup. Ct., 57 Cal.Rptr.2d 674, 680-1 (1996).

The California Supreme Court noted that "various studies show that arbitration is advantageous to employers . . . because it reduces the size of the award that an employee is likely to get, particularly if the employer is a 'repeat player' in the arbitration system." (citations omitted). *Armendariz v. Foundation Health,* 99 Cal.Rptr.2d 745, 768, 24 Cal.4th 83, 115 (2000).

Our Founders realized that the appearance of self-interest can and will jeopardize the public good, including the ability to preserve reserved rights of sovereignty and freedom of conscience. "No man is allowed to be a judge in his own cause, because his interest would certainly bias his judgment and, not improbably, corrupt his integrity." The Federalist No. 10, at 79 (James Madison) (Clinton Rossiter ed., 1961). A mandatory arbitrator's self-interest in protecting and promoting repeat business is at least apparent.

Every American must have the right to retain and choose a sovereign form of justice administration that has been deemed by our Founders to be the most impartial. It was the Framers' intent to maintain the civil jury as the cheapest, most expeditious and most impartial method of administering justice. It was not their intent to have a self-interested form of arbitration, unchecked by the sovereign, replace the civil jury system as the favored, cheapest, most impartial and most expeditious form of justice. The republican answer lies in the simplification of civil procedure and jury trials, not in the latter's compelled annihilation by *mandatory* arbitration.

II. CALIFORNIA HEALTH & SAFETY CODE §1363.1 IS A STATUTE THAT REGULATES THE BUSINESS OF INSURANCE PURSUANT TO THE MCCARRAN-FERGUSON ACT AND THEREFORE REVERSE PREEMPTS THE FEDERAL ARBITRATION ACT

Pursuant to the FAA, voluntary agreements to arbitrate matters concerning interstate commerce are enforceable. However, reverse preemption under McCarran-Ferguson creates an important exception to this general rule, and this case falls squarely within that exception. The McCarran-Ferguson Act grants to each state the authority to regulate the business of insurance, including the circumstances under which an insurance company may, if at all, force its policyholders into compulsory arbitration. Moreover, McCarran-Ferguson forbids encroachment on that state control by federal legislation of general applicability, including the FAA. California law mandates that arbitration clauses in insurance agreements conform to the standard set forth in *California Health & Safety Code §1363.1.* Compelling arbitration under the FAA would impair California's laws regulating insurance, and thus the FAA's preemption of state law is itself reverse preempted by McCarran-Ferguson. This Court has previously denied certiorari on this exact issue. *Smith v. PacifiCare Behavioral Health of California, Inc.*, 93 Cal.App.4th 139, 113 Cal.Rptr.2d 140 (2001), *cert. denied*, 537 U.S. 818 (2002).

The Federal Arbitration Act creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate. *See, Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 25 (1983). The FAA provides that an arbitration agreement "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation

of any contract." *9 U.S.C. Section 2.* Normally, the FAA preempts a conflicting state law that prohibits arbitration.

However, the court must consider the impact of the McCarran-Ferguson Act, which was enacted to "restore the supremacy of the state in the realm of insurance regulation." *U.S. Dept. of Treasury v. Fabe*, 508 U.S. 491, 500 (1993). "[N]o Act of Congress shall be construed to invalidate, impair or supercede any law enacted by any state for the purpose of regulating the business of insurance . . . unless such act specifically relates to the business of insurance . . ." *15 U.S.C. Section 12(b).* The courts have found that the McCarran-Ferguson Act reflects "firm congressional intent to leave regulation of the insurance industry primarily to the states." *Steffens v. National Distillers and Chemical Corp.*, 69 F.3d 1226, 1228 (2nd Cir. 1995). "It is clear . . . that by this legislation, the congress established a public policy on the part of the national government to refrain from interfering with the regulation and taxation of insurance companies by the several states." *U.S. v. Sylvanus*, 192 F.2d 96, 100 (7th Cir. 1951). "Obviously, Congress' purpose was broadly to give support to the existing and future state systems of regulating and taxing the business of insurance." *Prudential Ins. Co. v. Benjamin*, 66 S.Ct. 1142, 1154 (1946). In reviewing state regulations there is a "reluctance to disturb state regulatory schemes." *SEC v. Variable Annuity Life Ins. Co. of America*, 359 U.S. 65, 68 (1959). In short, the act "indicates the special status of insurance in the realm of state sovereignty." *Munich American Reins. Co. v. Crawford*, 141 F.3d 585, 595 (5th Cir. 1998), *cert. denied*, 119 S.Ct. 539 (1998).

The McCarran-Ferguson Act reverses the usual preemptive effect of federal law. *Fabe*, 508 U.S. at 500; and *Munich Amer. Reinsur. Co. v. Crawford*, 141 F.3d 585, 590 (5th Cir. 1998). In the narrow range of cases involving

state regulation of the insurance industry McCarran-Ferguson clothes state legislation in federal garments. *Id.* Absent a Congressional act specifically relating to the business of insurance, McCarran-Ferguson provides that state law controls over conflicting federal legislation. *Id.*

California Health & Safety Code §1363.1 states in relevant part:

> Any health care service plan that includes terms that require binding arbitration to settle disputes and that restrict, or provide for a waiver of, *the right to a jury trial* shall [at a minimum] include, in clear and understandable language, a disclosure that meets all of the following conditions . . . [t]he disclosure shall clearly state whether the plan uses binding arbitration to settle disputes, including specifically . . . to settle claims of medical malpractice . . . [t]he disclosure shall appear as a separate article . . . prominently displayed on the enrollment form to be signed by each . . . enrollee . . . [t]he disclosure shall clearly state whether the . . . enrollee is waiving . . . *a jury trial* for medical malpractice, other disputes relating to the delivery of service . . . or both, and . . . shall be displayed immediately before the signature line provided . . . for the individual enrolling . . . (emphasis added).

Does California Health & Safety Code §1363.1 preempt the general application of the FAA under McCarran-Ferguson? For the reasons stated below, the answer is yes.

As construed by this Court, McCarran-Ferguson "precludes application of a federal statute in the face of state law when: (A) the federal statute is one of general applicability rather than one specifically related to the business of insurance; (B) the state statute regulates the business of insurance; and (C) application of the federal statute would invalidate, impair or supercede the state's law. *Humana Inc. v. Forsyth*, 525 U.S. 299, 307 (1999).

A. THE FAA IS A LAW OF GENERAL APPLICABILITY

The FAA is a federal measure not specifically related to insurance. *Davister Corp. v. United Republic Life Insurance Company*, 152 F.3d 1277, 1279 n.1 (10th Cir. 1998); "no one disputes the fact that the FAA does not specifically relate to insurance." *Stephens v. American Intl. Ins. Co.*, 66 F.3d 41, 44 (2nd Cir. 1995).

B. CALIFORNIA'S MANDATORY DISCLOSURE OF WAIVER OF THE CONSTITUTIONAL RIGHT TO COURT AND JURY ACCESS IS A STATE LAW REGULATING THE BUSINESS OF INSURANCE WITHIN THE MEANING OF THE MCCARRAN-FERGUSON ACT

In determining if a state law regulates the business of insurance, this Court has found three factors relevant: 1) whether the practice [state law] has the effect of transferring or spreading a policyholder's risk; 2) whether the practice is an integral part of the policy relationship between the insurer and the insured; and 3) whether the practice is limited to entities within the insurance industry. *Unum Life Ins. Co. of America v. Ward*, 526 U.S. 358, 367 (1999). The three factors are "considerations [to be] weighed" in determining whether a state law regulates insurance and "[n]one of these criteria is necessarily determinative in itself." *Id.* at 373. The factors are checking points or guide posts, not separate essential elements. *Id.* at 374. All the factors need not point in the same direction. *Id.*

1. CALIFORNIA HEALTH AND SAFETY CODE §1363.1 TRANSFERS OR SPREADS POLICYHOLDER RISK BETWEEN THE POLICYHOLDER AND THE INSURER

By attempting to make arbitration mandatory, CIGNA transferred or spread the risk of Muzeyyen Balaban-Zilke's claims, and the enforcement costs connected therewith, from the insurance company to the insured. By interjecting the possibility of a civil trial and jury award for non-compliance with its statute, California has substantially altered the risk assumed by the parties, shifting it back to the insurance company. "To expressly invalidate an agreement contained in the insurance contract touches the core of 'the business of insurance.'" *Mutual Reinsurance Bureau v. Great Plains Mut. Ins. Co.,* 969 F.2d 931, 933 (10th Cir. 1992). Thus, the requirements of *California Health & Safety Code §1363.1* protects insureds from the insurance companies' attempt to spread the risk and cost of enforcement from the insurance companies to the insureds through compelled arbitration.

CIGNA argues that *California Health & Safety Code §1363.1* does not "substantially affect the risk pooling arrangement between the insurer and the insured" (Pet. brief at page 11), and would therefore fail the second prong of the test articulated in *Kentucky Ass'n of Health Plans v. Miller*, 123 S.Ct. 1471 (2003). While acknowledging that *Miller* was decided in an ERISA context, CIGNA does not acknowledge that this Court "makes a clean break from McCarran-Ferguson factors" in decisions relating to state laws regulating insurance under ERISA's savings clause. *Miller,* 123 S.Ct. at 1479.

CIGNA's conclusory pronouncement that *California Health & Safety Code §1363.1* does not substantially affect the risk pooling arrangement between the insurer and the insured (Pet. brief at page 11) belies its own actions. It is

disingenuous of CIGNA to argue that the consequences of non-compliance with *California Health & Safety Code §1363.1* does not affect their risk, while concurrently pursuing appeals through three courts. (Pet. brief at page 1). Numerous commentators have noted that "insurance premiums . . . rise conversely with an increase in the number of suits brought." Alan Feigenbaum, *Special Juries: Deterring Spurious Medical Malpractice Litigation in State Courts*, 24 Cardozo L. Rev. 1361, 1364 (2003). "General counsels of health care organizations . . . know that litigation driven dispute resolution is a 'hidden culprit' in rising insurance costs." Karl A. Slaikeu and Diane W. Slaikeu, *Confidential from General Counsel to Ceo: "I'm Fed Up, and We're Not Going to Take This Anymore!"*, 5 J. Health Care L. & Pol'y 335 (2002). [Respondent believes the actual effect of litigation of disputes would lower premiums, in that Superior Court Judges are free, while private arbitrators charge $5,000.00 to $7,500.00 per diem].

CIGNA would have this Court believe that not being able to compel arbitration would have no substantial effect on their risk pooling arrangement, yet this issue is worthy of three appeals.

As the Chair of the Subcommittee on the Constitution of the Senate Committee on the Judiciary has observed: "Regrettably, with the help of the federal courts, powerful institutions are subverting Congress' original intention in passing the FAA. Instead of providing disputants with options for dispute resolution, the courts and these institutions are converting arbitration into a tool for the powerful to exert authority over the less powerful. Thus, many people are essentially forced to forgo constitutional rights when disputes arise relating to their jobs, businesses, and finances" [and in Respondent's experience their very lives]. Senator Russell D. Feingold, *Mandatory Arbitration: What Process Is Due?*, 39 Harv. J. on Legis. 281, 284 (2002).

2. CALIFORNIA HEALTH & SAFETY CODE §1363.1 AFFECTS AN INTEGRAL PART OF THE POLICY RELATIONSHIP BETWEEN THE INSURER AND THE INSURED BY PROTECTING THE POLICYHOLDERS' INTEREST & CONTROLLING THE TERMS OF THE CONTRACT

This Court in *Fabe* specifically held that laws concerning the "end intention or aim of adjusting, managing or controlling the business of insurance came within the meaning of the McCarran-Ferguson Act." *U.S. Dept. of the Treas. v. Fabe,* 508 U.S. 491, 505 (1993). This reasoning is consistent with the purpose of the McCarran-Ferguson Act which was enacted to preserve the states' authority to protect policyholders from overreaching conduct by insurance companies. A state statute aimed at protecting the relationship between the insurer and the insured is the "focus of McCarran-Ferguson." *Fabe,* 508 U.S. at 501. *Fabe*'s reasoning is also consistent with *SEC v. National Securities, Inc.*, 393 U.S. 453 (1969). As one District Court noted, this Court made clear that: the "*Fabe* holding . . . is a broader interpretation of the Supreme Court's prior holding in *SEC v. National Securities, Inc.* [citation omitted] Thus, the *Fabe* holding attempts to give meaning to the plain words of the McCarran-Ferguson Act by exempting any state law which directly or indirectly assists policyholders from federal preemption." *Boozell v. United States*, 979 F. Supp. 670, 678 (N.D. Ill. 1997).

"Statutes aimed at protecting or regulating this [policyholder-insurance company] relationship, directly or indirectly are laws regulating the 'business of insurance.'" *SEC v. National Securities, Inc.*, 393 U.S. 453, 460 (1969); *See also, Zelson v. Phoenix Mut. Life Ins. Co.*, 549 F.2d 62, 68 (8th Cir. 1977) ("the insurer-policyholder relationship is at the 'core' of the insurance business."); *Mathis v. Auto*

Club Inter-Insurance Exchange, 410 F. Supp 1037, 1040 (W.D. Mo. 1976) ("If the state 'has generally authorized or permitted certain standards of conduct' in the insurer-insured relationship . . . [the state] . . . is regulating the business of insurance within the meaning of [the] McCarran-Ferguson Act.")

Expounding upon the holding in *National Securities* in *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 215 (1979), this Court stated, "Another commonly understood aspect of the business of insurance relates to the contract between the insurer and the insured." California's necessitation of clear and prominent disclosure and consent to mandatary arbitration in contracts of insurance was clearly enacted to adjust or manage the enforceable terms of the agreement between the insurer and the insured.

By adjusting or managing the terms of enforcing the agreement, California law has transferred or spread the risk. Under the holding of *Fabe* and other Supreme Court decisions, *California Health & Safety Code §1363.1* was enacted for the purpose of regulating the business of insurance. *See, Unum*, 526 U.S. at 374. (Rule that "has the effect of raising premiums" spreads risk among policyholders.) Here, *California Health & Safety Code §1363.1* provides the enrollee with notice of a potentially offensive arbitration clause prior to enrollment; therefore, the enrollee may competitively opt for a different plan of insurance without this clause [presuming such an option is available]. Hence, there is an inherent business risk to the insurer that the potential enrollee will "vote with his feet," and take his premium dollars elsewhere, thus reducing market share and the available risk pool. This too "spreads or transfers" risk.

Finally, as held in *Unum*, when the two other factors of McCarran-Ferguson are met, it need not be determined

that the 'risk spreading' factor be satisfied. *Johnston v. Paul Revere Life Ins. Co.*, 241 F. 3d 631, 623 n. 9 (8th Cir. 2001) (citing *Unum* at 360.)

3. THE PROVISIONS OF CALIFORNIA HEALTH & SAFETY CODE §1363.1 ARE EXCLUSIVELY LIMITED TO ENTITIES WITHIN THE INSURANCE INDUSTRY

California Health & Safety Code §1363.1 states in pertinent part that: "Any health care service plan that includes terms that require binding arbitration . . ." is the object of its application. Petitioner CIGNA concedes that Respondent "could not have obtained coverage" without signing a mandatory arbitration clause. (Pet. brief at page App. 16). CIGNA admits and recognizes that it is a "health care service plan" within the ambit of this statute and the McCarran-Ferguson Act. (Pet. brief at page 5) *See also, Rush Prudential HMO, Inc. v. Moran,* 536 U.S. 355 (2002). Therefore, Petitioner is a legitimate object of the statute's reach.

The statute appears in "Health and Safety Code, Division 2. Licensing Provisions, Chapter 2.2 Health Care Service Plans, Article 4. Solicitation and Enrollment." *West's Annotated California Codes* (2003). By its own clear language and location, the statute is applicable only to health care service plans, and hence limited to entities within the insurance industry.

CONCLUSION

California Health & Safety Code §1363.1 requires clear and prominent disclosure, in statutorily proscribed language, necessitating the consent of an insured to mandatory arbitration in health care service contracts. Under the McCarran-Ferguson Act, the FAA is reverse

preempted because a law of general applicability such as the FAA may not be applied to defeat the state's control in the area of regulating the insurance industry.

This Court has been briefed, and denied review, on this identical issue, *Smith v. PacifiCare Behavioral Health of California, Inc.*, 93 Cal.App.4th 139, 113 Cal.Rptr.2d 140 (2001), *cert. denied*, 537 U.S. 818 (2002) (non-compliance with *California Health & Safety Code §1363.1* bars enforcement of arbitration clause, FAA reverse preempted by McCarran-Ferguson). Though Petitioner has couched its argument in the guise of a split in authority regarding the FAA and the McCarran-Ferguson Act – ERISA, RICO, the SEC, Bankruptcy, Third-party, and the litany of 33 cases and 20 statutes string cited (Pet. brief at pages 5-7) are not the issue(s) presented by this case and therefore should not be considered by this court.

Artfully pled, expensive and exhaustive appellate fighting encouraged by the insurance industry [such as the record here], dissuades many plaintiff's attorneys from accepting otherwise worthy cases. This not only reduces the pool of counsel, but also the actual number of cases prosecuted.

California has recognized that direct democratic lawmaking through the initiative and referendum process is part of a "republican form of government." *In re Pfahler*, 88 P. 270, 150 Cal. 71 (1906). The civil jury, consisting of the sovereign, also represents direct democratic participation, but in the administration of laws and justice. For this reason, California has recognized that the civil trial by jury is the "strongest safeguard of the liberty of the citizen (be he high or low, rich or poor) against encroachments upon his freedom caused by firebrands, demagogues, or regnants exercising their influence over the people through democratic, bureaucratic, or republican forms of

government." *Union Oil Co. of California v. Hane*, 80 P.2d 516, 519, 27 Cal.App.2d 106, 111 (1938).

Review should be granted by this Court, but not on the grounds asserted by Petitioner here. Rather, review should be granted based upon the Republican grounds analyzed under Section I herein. The Federal government, under *9 U.S.C. §2*, empowered State governments, as it was constitutionally required to do, to rely on State standards to revoke contracts of adhesion "upon such grounds as exist at law or equity," whenever those contracts violate an individual's preexisting and superior substantive due process right to choose.

Respectfully submitted,

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Attorneys for Respondent Muzeyyen Balaban-Zilke, Ph.D., Individually and as Successor-in-interest to Brad Zilke

* *Counsel of Record*

DECLARATION OF NIDU PERMAUL

I, NIDU PERMAUL, do hereby declare and state as follows:

1. I am currently employed with the County of Los Angeles ("County"). I have worked for the County for the last thirty-four and one-half (34½) years. I have been the Principal Human Resource Analyst since 1996. For the preceding five (5) years, I was the Assistant Principal Resource Analyst. These positions are in Benefits Administration. My business address is 3333 Wilshire Boulevard, 10th floor, Los Angeles, California.

2. I have first hand personal knowledge of the matters stated herein and could and would competently testify thereto under oath if called as a witness. I make this Declaration in support of the Motion for Reconsideration submitted by CIGNA Healthcare of California, Inc. ("CIGNA") regarding their Petition to Compel Arbitration.

3. My duties as a Principal Human Resource Analyst involve providing day to day supervision of benefit operations including contract administration, communication with employers, participation in the enrollment process and problem resolution, solely with respect to insurance benefits for the County of Los Angeles which has approximately 80,000 employees. As an Assistant Principal Human Resource Analyst, I assisted the Principal Human Resource Analyst in performing the same duties for five years.

4. As part of my job responsibility, I oversee and maintain as custodian the contracts between the County and various health care providers, including CIGNA Healthcare of California, Inc.

5. Attached hereto as Exhibit "A" is a true and correct copy of the complete, executed 1991 Contract between CIGNA HealthCare of California, Inc. and the County of Los Angeles.

6. Attached hereto as Exhibit "C" is a true and correct copy of the complete, executed 1993 Amendments to the 1991 Contract between CIGNA HealthCare of California, Inc. and the County of Los Angeles.

8. Attached hereto as Exhibit "D" is a true and correct copy of the complete, executed 1996 Contract between CIGNA HealthCare of California, Inc. and the County of Los Angeles.

9. Attached hereto as Exhibit "E" is a true and correct copy of the complete, executed 1997 Contract between CIGNA HealthCare of California, Inc. and the County of Los Angeles.

10. In 1992, the County gave all of its new employees a packet of materials upon being hired. This packet included information about the various health plans with which the County had contracted to provide health care benefits to its employees. This packet also included an enrollment application for health care coverage. A true and correct copy of the enrollment application utilized in 1992 by the County is attached hereto as Exhibit "F".

11. The enrollment application utilized by the County in 1992 states, "I understand that I must abide by the provisions of the plan(s) in which I enroll, and that enrollment in Kaiser, some CIGNA plans and ALADS CaliforniaCare or any other County-approved Health Maintenance Organization plan constitutes an agreement to have any issue of medical malpractice decided by

arbitration and waiver of any right to a jury or court trial." (Emphasis added.)

12. At times relevant hereto Department policy has required that once an employee has completed the enrollment application, it is maintained by the County of Los Angeles. The health care provider, such as CIGNA, does not get a copy of the County's signed enrollment application. Furthermore, there were no separate enrollment applications in 1992 to be completed by County employees for CIGNA.

13. The County of Los Angeles only keeps enrollment applications for a period of five (5) years. Thereafter, they are destroyed in the routine course of business. Accordingly, enrollment applications completed in 1992 were destroyed in 1997 pursuant to our departmental policy.

14. In 1992, an employee of the County could not obtain health care coverage until he or she first completed and signed an enrollment application, such as the one attached hereto as Exhibit "F".

15. At or about 1995, the County of Los Angeles began providing health care benefits for domestic partners of its employees. Domestic Partners also completed an enrollment form. A true and correct copy of the Domestic Partner Enrollment and Change Form actually utilized by the County in 1996 is attached hereto as Exhibit "G".

16. The Enrollment Form, which requires the signature of both the County employee and the domestic partner states, "I understand that if I enroll in any HMO plan (such as Kaiser, the CIGNA Medical Group, Network model or Health Access plans; or the FHP/TakeCare HMO or Low Option HMO plans; or the Health Net HMO, etc.)

I waive any right to a jury trial and agree to have any issue of medical malpractice decided by arbitration." (Emphasis added.)

17. No domestic partner would be eligible as of 1996 to receive health care coverage from CIGNA or any other health care provider until he or she first completed and signed the Domestic Partner Enrollment Form, such as the one attached hereto as Exhibit "G". To receive coverage through CIGNA as a domestic partner of a County employee as of 1996, both the employee and domestic partner must have signed an enrollment form such as the one attached hereto as Exhibit "G".

18. I am not at liberty to attach the completed enrollment form of Brad Zilke to this declaration without his (or his representative's) authorization, proper subpoena or court order.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed this 25 day of February, 2000 in Los Angeles, California.

/s/ Nidu Permaul
NIDU PERMAUL

DOMESTIC PARTNER ENROLLMENT AND CHANGE FORM	
Employee Name (Last, First/Initial)	***Employee Number***

If you are enrolling your domestic partner in your medical and/or dental plan, place a "Y" in the Medical and/or Dental column. If you are removing him/her from your medical and/or dental plan, place an "N" in the Medical and/or Dental column(s). (To add domestic partner you must submit a Declaration of Domestic Partnership form and removal requires you to submit a Termination Domestic Partnership form. Call the Benefits Plan Administrator at (310) 397-7220.)

Domestic Partner Name and Information (PLEASE PRINT)			
Name (Last, First/Initial)	***Sex M/F***	***Birth Date***	***Medical Y/N***

Medical Group/Physician Name/Number	***Dental Y/N***	***Dentist No. (Safeguard only)***	***Social Security #***

If you are enrolling a child of your domestic partner, write in the name and other required information below; place a "Y" in the Medical and/or Dental column. To remove a child from coverage, write in the name and date of birth of the child and place an "N" in Medical and/or Dental column.

Name(s) & information of Domestic Partner's Dependent Child(ren) (PLEASE PRINT)			
Name (Last, First/Initial)	***Sex M/F***	***Birth Date***	***Medical Y/N***

Medical Group/Physician Name/Number	***Dental Y/N***	***Dentist No. (Safeguard only)***	***Social Security #***

If you are enrolling a dependent child, you must provide proof that the child is a legal dependant of your domestic partner. This proof must be received by the LA County Benefits Plan Administrator at the address below along with the enrollment form. The following documents are required to certify the dependent status of a child:

Child(ren) . . . . Hospital or state birth certificate or legal adoption papers.

Student(s) . . . . Ages 19 to 25, written certification of full time status from a college or university (e.g., letter from school/school registration).

Disabled child . . . . Certification of total disability by a qualified physician.

I understand that if I enroll in any HMO plan (such as Kaiser, the CIGNA Medical Group, Network model or Health Access plans; or the FHP/TakeCare HMO or Low Option HMO plans; or the Health Net HMO, etc.) I waive any right to a jury trial and agree to have any issue of medical malpractice decided by arbitration.

We declare under penalty of perjury that the foregoing is true and correct.

Domestic Partner Signature _____ Date _____

Employee Signature _____ Date _____

Sign and date this form and mail it with your Declaration *and any required certificates* described above to:

County of Los Angeles Benefits Plan Administrator
P.O. Box 34050
Los Angeles, CA 90034

DECLARATION OF MUZEYYEN BALABAN-ZILKE

I, Muzeyyen Balaban-Zilke hereby declare as follows:

1. I am a party to this action and have personal knowledge of the facts stated herein. If called as a witness, I could and would testify under oath as to the contents of this Declaration.

2. I have been employed by the County of Los Angeles, Department of Children and Family Services since 1992. I enrolled in a CIGNA health care service plan that year and was a member of a CIGNA plan throughout the illness of Brad Zilke, my now deceased husband. Brad was also covered under the plan. Specifically, I obtained medical insurance for Brad and me through a group health plan obtained through my place of employment, beginning in 1992 and continuing year to year thereafter.

3. At no time was I ever given any brochures which disclosed to me that CIGNA used binding arbitration to settle disputes, nor was I told that I was giving up my right to a jury trial by enrolling in a CIGNA health plan. I also do not recall signing any enrollment form on which there was language concerning arbitration and I do not believe I ever saw or signed any such form. Even as of this time, I am unaware of any arbitration language being on any enrollment form provided to me. If such language is on any enrollment form, then it was not conspicuously placed. Had such language been conspicuous, I would have seen it and would have been in a position to object to it or to enroll in another health care plan.

4. Throughout the entire time Brad was ill and unsuccessfully trying to obtain proper care from CIGNA, I was unaware of any contract or agreement which provided

for arbitration. CIGNA never advised Brad or I of the existence of any right to participate in an arbitration proceeding, nor were we told how to initiate such a proceeding, to the extent it may have been available. Neither CIGNA nor any CIGNA representative ever discussed arbitration with me.

5. During the time of our medical coverage disputes with CIGNA, Brad and I had a number of conversations with CIGNA's gatekeeper Victor Gura, M.D. in which he repeatedly mentioned economic concerns as reasons for not authorizing comprehensive follow-up tests for Brad after a mole containing malignant melanoma was removed in 1996. At one point, Dr. Gura said, "What do you think we are, a bank" and "You have cheap insurance and we can't afford to give you a CT scan," and "We don't do this for simple melanomas." Dr. Gura kept fighting us and Brad did not obtain all of the necessary tests. At that time, our focus was on saving Brad's life, and we were in no position to resort to lengthy and expensive litigation in order to obtain the medical coverage benefits which CIGNA should have provided. We were never told that the CIGNA health plan had an arbitration process which could be used to expeditiously resolve medical coverage issues.

6. Although CIGNA declined to authorize certain medical treatment for Brad, it never mentioned any recourse either Brad or I may have had under any arbitration clause. CIGNA did not timely or adequately apprize Brad or I about any availability of arbitration, nor did CIGNA mention arbitration at all. I believe that Brad died because CIGNA and the other defendants failed to timely provide the treatment which Brad needed. Had CIGNA told us that we had recourse to a prompt and informal

means of resolving coverage issues with CIGNA through arbitration, we would have tried to invoke that procedure at a period of time when full and proper treatment could have saved Brad's life. However, I was not aware that CIGNA contended arbitration was an available remedy to Brad or me.

7. It was only after this lawsuit was filed in April, 1999, that I first became aware that CIGNA claimed that an arbitration clause existed which affected my rights and Brad's rights. I first learned this from an attorney which I retained following Brad's death, and not from any CIGNA representative. Prior to that time, I was unaware of any arbitration clause in CIGNA's agreements and I never knowingly consented to have my claims determined by arbitration, nor was I ever advised during Brad's lifetime that arbitration was available to Brad and me to attempt to obtain benefits under the CIGNA health plan or to otherwise vindicate our rights against CIGNA.

8. I have never knowingly consented to having my disputes with CIGNA arbitrated, nor have I consented to give up my right to have a jury hear and determine my claims arising from the death of my husband. As I stated earlier, I was not even made aware of any arbitration clause with CIGNA until after this case was filed.

9. I am informed that CIGNA has relied on a 1998 arbitration agreement in order to attempt to compel arbitration of my individual claims and those I am making as successor-in-interest to Brad. Although Brad died in November, 1998, most or all of the improper conduct and treatment upon which this action is based occurred prior to 1998. I did not retroactively agree to arbitrate disputes with CIGNA based on treatment previously rendered or

other conduct by CIGNA prior to 1998. As of 1998, Brad's medical condition was irreversible. Had I been asked in 1998 or thereafter to agree to arbitration of such claims, and had I understood what was being asked of me, I would have certainly declined.

I declare under penalty of perjury under the laws of the United States and the State of California that the foregoing is true and correct.

Executed on January 11, 2000, in Los Angeles, California.

/s/ M. Balaban-Zilke
MUZEYYEN BALABAN-ZILKE

No. 03-709

Supreme Court, U.S.
FILED
DEC 2 3 2003
OFFICE OF THE CLERK

In The Supreme Court of the United States

CIGNA HEALTHCARE OF CALIFORNIA, INC.,

Petitioner,

vs.

MUZEYYEN BALABAN-ZILKE, Ph.D., individually and as successor-in-interest to BRAD ZILKE,

Respondent.

On Petition For A Writ Of Certiorari To The Court Of Appeal Of California, Second Appellate District

PETITIONER'S REPLY MEMORANDUM

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PETITIONER'S REPLY MEMORANDUM

In her opposition brief, respondent agrees with petitioner that "[r]eview should be granted by this Court" and raises an additional issue for this Court to consider – whether an arbitration agreement contained in a standard form contract of adhesion represents an unconstitutional deprivation of the right to a jury trial. Br. in Opp'n at i, 2-19, 30. Respondent's opposition confirms that this Court should grant CIGNA's petition for writ of certiorari to resolve the numerous conflicts in authority regarding application of the McCarran-Ferguson Act to the Federal Arbitration Act identified in CIGNA's petition. Respondent's new issue, however, does not present any question requiring resolution by this Court.

First, to the extent respondent argues it is unconscionable to allow a contracting party to give up the right to a jury trial, that issue is not properly presented by this record. In this case, the California Court of Appeal did not hold that CIGNA's arbitration contract ran afoul of generally-applicable state laws regarding unconscionability and contracts of adhesion. Pet. App. at 4-5. Instead, the Court of Appeal refused to enforce the contractual arbitration clause solely on the basis of a state law (Cal. Health & Safety Code § 1363.1 (West 2000)) that set special conditions for the enforcement of any arbitration agreements contained in a healthcare plan. Pet. App. at 4-6.

Second, this Court has previously enforced other arbitration contracts found in similar standard form contracts. *See, e.g., Doctor's Assocs. v. Casarotto*, 517 U.S. 681, 682, 686-87 (1996); *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 268-69, 280-81 (1995). It appears to be settled law that there is nothing inherently unconscionable

about agreeing to forego a jury trial in favor of alternate dispute resolution.

Third, the California and Ninth Circuit opinions cited by respondent in support of her new issue all reinforce CIGNA's point that, on a variety of grounds, lower courts are refusing to enforce contractual arbitration agreements for reasons that cannot be squared with the Federal Arbitration Act. *See, e.g.*, Br. in Opp'n at 10-14, 19; *Circuit City Stores, Inc. v. Mantor*, 335 F.3d 1101, 1107-09 (9th Cir. 2003); *Armendariz v. Found. Health Psychcare Servs.*, 24 Cal. 4th 83, 120-21, 99 Cal. Rptr. 2d 745, 771-73 (2000); *Broughton v. Cigna Healthplans*, 21 Cal. 4th 1066, 1082-85; 90 Cal. Rptr. 2d 334, 346-48 (1999). Respondent's authority shows that many courts do not place arbitration contracts " 'upon the same footing as other contracts' " and improperly "invalidate arbitration agreements under state laws applicable *only* to arbitration provisions." *Doctor's Assocs.*, 517 U.S. at 687. Respondent's authority thus provides additional support for CIGNA's petition because it demonstrates the urgent need for this Court to clarify the extent to which federal law requires enforcement of arbitration agreements, and whether it is permissible for courts to deny enforcement of such contracts on the basis of their manifest hostility toward arbitration agreements.

Respectfully submitted,

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Supreme Court, U.S.
FILED
JAN 28 2004
OFFICE OF THE CLERK

No. 03-709

In The Supreme Court of the United States

CIGNA HEALTHCARE OF CALIFORNIA, INC.
(Erroneously sued as CIGNA HEALTHCARE, INC. and CIGNA HEALTHPLANS OF SOUTHERN CALIFORNIA),

Petitioner,

vs.

MUZEYYEN BALABAN-ZILKE, Ph.D., individually and as successor-in-interest to BRAD ZILKE,

Respondent.

On Petition For A Writ Of Certiorari To The Court Of Appeal Of California, Second Appellate District

PETITION FOR REHEARING PENDING RESOLUTION OF RELATED PETITION FOR WRIT OF CERTIORARI

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PETITION FOR REHEARING

Petitioner CIGNA HealthCare of California, Inc. (CHC) respectfully moves this Court for an order (1) vacating its denial of the petition for writ of certiorari entered on January 12, 2004, and (2) granting the petition.

This Court should grant CHC's petition for rehearing if it grants the pending petition for writ of certiorari in *Allen v. Pacheco*, 71 P.3d 375 (Colo. 2003), *petition for cert. filed,* 72 U.S.L.W. 3310 (U.S. Oct. 28, 2003) (No. 03-642) which raises the identical question presented by CHC's petition. *See, e.g., Simmons v. Sea-Land Servs. Inc.*, 462 U.S. 1114 (1983) (rehearing granted and case remanded in light of Supreme Court opinion in a related case); *Florida v. Rodriguez*, 461 U.S. 940 (1983) (same); *Forgett v. United States*, 390 U.S. 203 (1968) (same).

The state courts in *Allen* and *Balaban-Zilke* both refused to enforce arbitration agreements in health care plans because the agreements did not meet special requirements set by state law. *Compare Balaban-Zilke v. CIGNA HealthCare of Cal., Inc.*, No. B140672, 2003 WL 21228038, at *2-6 (Cal. Ct. App. May 28, 2003) *and* Cal. Health & Safety Code § 1363.1 (West 2000), *with Allen v. Pacheco*, 71 P.3d 375, 377 (Colo. 2003) *and* Colo. Rev. Stat. § 13-64-403 (2003). Both petitions present the identical "reverse preemption" question – whether the McCarran-Ferguson Act saves state laws that impose special requirements on arbitration agreements in health care plans from preemption by the Federal Arbitration Act. *See* CHC's Pet. at i; Allen's Pet. at i.

If this Court grants the petition for writ of certiorari in *Allen v. Pacheco*, it should also grant CHC's petition.

Respectfully submitted,

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Attorneys for Petitioner CIGNA HealthCare of California, Inc. (Erroneously sued as CIGNA HealthCare, Inc. and CIGNA Healthplans of Southern California)

CERTIFICATE OF COUNSEL

As counsel for the petitioner, I hereby certify that this petition for rehearing is presented in good faith and not for delay and is restricted to the grounds specified in Rule 44(2) of the Rules of this Court.

JEREMY B. ROSEN